

# INVESTMENT CLIMATE AND TREND OF FOREIGN INVESTMENT IN BANGLADESH : A STUDY OF JAPANESE INVESTORS<sup>1</sup>

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## INTRODUCTION

Bangladesh with its 120 million people has the highest population density in the world, yet enjoys many strengths-particularly its potential consumer market in the garment industry, leather goods and shrimp farming. Real GDP growth has been steady and more remarkably it has managed to achieve near self sufficiency in foodgrains production. Since 1991 the Government has embarked on a successful macro-economic stabilization programme with the improvement in balance of payments, increase in foreign exchange reserves and exports.

Against this backdrop of economic achievement a market friendly and deregulated environment entice investors around the world. Bangladesh has enjoyed spectacular growth in foreign direct investment, particularly in recent years. During 1947-1971 in pre-liberation days, investment totalled just US \$40 million. Over the next 19 years, between 1972 and 1991 the amount had increased only to \$ 389 million. But from 1991 to 1997, foreign direct investment jumped to well over 3548 million US dollars. This dramatic increase indicates the adaptability of the country in creating an investment climate sought by international investors.

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The government's focus on economic liberalization has created liberal policy reforms, incentive package and associated benefits, to create conducive conditions for the successful growth of industries through both local and foreign investment. A solid economic and political atmosphere has been established for foreign investment with the necessary legal protection, administrative reorganization and attractive incentive packages. Moreover, the country has embarked on an ambitious privatization programme offering substantial opportunities for international investors.

The purpose of his paper is to provide an overview of investment climate and trend of foreign investment in Bangladesh with a focus on Japanese investors. This study is based on a survey carried out among the Japanese investors in Bangladesh which aimed at finding out the perceptions, problems and views of foreign investors in the country.

### **Investment Climate in Brief**

Perhaps, Bangladesh's best attraction for investors is its open door investment policy. The country has the most liberal investment climate in Asia. For instance, it takes just three days for a foreign investment registration and there is no discrimination between foreign and local private investors. Total (100%) foreign investment is allowed, as well as joint ventures with local partners, private or public.

To attract foreign investors, the government has offered the following of incentives.

- no ceiling on investment ;
- tax holidays of up to 12 years ;
- tax-exemption and duty free importation of capital machinery and spare parts for 100% export oriented industries ;
- residency permits for foreign nationals ;
- capital, profit and dividend repatriation facilities ;
- double-taxation avoidance ;

- tax-exemption on the interest payable on foreign loans ;  
open exchange controls

All sectors of industry (barring five reserved for public sector) are open for private investment. The five sectors reserved for public investment are : defence and defence production, nuclear energy, extraction from reserved forests, security printing and mint, and air transportation and railways. However, lately some private airlines have been allowed on domestic routes and several railway routes have also been handed over to private operators. Foreign investment is particularly welcome in the export-oriented industries such as textiles, leather goods, electronic products and components, chemicals and petrochemicals, agro-based industries, mining, green jute, pulp, paper, and rayon products. Investors are also welcome into the telecommunications and power generation sectors. The government is also keen to encourage investment in the country's infrastructure such as toll-ways, highways and roads. Other areas are modernization of the jute goods sector (Bangladesh is one of the leading producers in the world) ; frozen foods (dominated by shrimp farming); tourism and agriculture and data processing. Foreign investment is also desired in high technology products that will help import substitution labour and technology intensive of industries.

A number of prestigious blue-chip foreign companies have invested in textiles, steel mills and hotels. Names like Nestle, Singer, Lever Brothers, Hoechst, Rhone-Poulenc, Cairn Energy, Hutchinson, Marubeni and Chiyoda have taken up opportunities in manufacturing, energy and telecommunications sectors.

### **Trends of Foreign Investment in Bangladesh**

Foreign Direct Investment (FDI) inflows are accompanied by better training and entrepreneurial abilities of foreign entrepreneurs and lead to general improvements in the managerial standards of the

host countries. FDI has proved a very effective means of transfer of technology from the developed to developing countries. FDI helps improve both internal marketing and overseas distribution networks which may possibly help increase earning.

Foreign investment in the industrial sector has been increasing over the years and has taken place through establishment of fully foreign owned enterprises or participation in joint ventures and through portfolio investments through the country's stock markets. Board of Investment (BOI) maintains records on investments registered with them.

Table-1 shows total investments registered with BOI over the years (1991/92 to 1995/96). It is observed that total investment registered with BOI rose from US \$ 116 million during 1991-1992 to US \$ 1574 million during 1994-95. During the period, foreign investment increased from US \$25 million to US \$729 million. Table-2 shows FDI flow from the year 1991/92 to year 1996-97

Table-1 : Investments Registered by BOI 1990/95

(in million US \$)			
Year	Local	Foreign	Total
1991/92	91	25	116
1992/93	90	53	143
1993/94	457	804	1,261
1994/95	845	729	1,574
1995/96	775	916	1,691
<b>Total</b>	<b>2,258</b>	<b>2527</b>	<b>4,785</b>

Source : Board of Investment (BOI), Bangladesh.

Table-2 : Foreign Direct Investment  
(1990/91 to February 1997)

(In million US.\$)

Country	1990 /91	1991 /92	1992 /93	1993 /94	1994 /95	1995 /96	1996/97 (Feb.'97)	Total
Malaysia	-	-	-	270.0	140.0	531.00	-	941.00
Japan	2.0	1.0	2.0	5.0	84.0	612.00	4.46	755.46
Hongkong	70.5	2.5	0.5	1.0	110.3	-	16.90	201.70
U.K.	0.8	3.0	2.0	72.0	51.5	70.00	31.90	231.20
India	0.5	1.0	0.2	10.7	117.0	8.00	27.75	165.15
Germany	2.0	1.0	0.4	4.0	56.5	65.00	8.42	137.32
U.S.A	-	-	1.5	2.4	13.0	47.00	5.60	69.50
Singapore	0.2	2.0	20.0	1.0	53.0	0.60	18.10	94.90
S. Korea	1.4	0.4	6.5	20.0	36.00	30.00	78.00	172.80
China	.05	-	1.0	25.0	12.2	0.40	8.82	47.52
Greece	7.4	-	-	-	12.0	5.00	-	24.40
Switzerland	-	10.0	-	-	0.3	3.60	2.26	16.16
Netherlands	6.0	1.5	-	-	1.2	5.00	-	13.70
Italy	-	0.8	0.5	0.3	1.5	-	2.80	5.90
Canada	-	-	-	-	0.3	0.70	4.25	5.25
Sweden	-	0.5	-	0.3	-	-	0.26	1.06
Others	1.0	1.5	18.0	347.5	40.6	123.70	118.95	651.25
Total	92.3	25.2	52.6	804.2	729.4	1516.00	329.00	3548.30

Source : Board of Investment, Bangladesh.

## A Study of Japanese Investors in Bangladesh

An investment climate survey was conducted to find out/identify the problems faced by Japanese firms already doing business in Bangladesh and know their views about the prospect of attracting further foreign investment in the country. In this respect suggestions and recommendations were sought from the Japanese firms.

### Brief Analysis of the Survey

It was observed from the survey that the investment trend between late 1980's and early 1990's from Japan did not continue due to three main reasons :

- (a) flood and cyclone of 1991 that seriously affected many Japanese investment in Chittagong,
- (b) continuous political disturbances (general strike or "Hartal") which created bad **image of Bangladesh in Japan and**
- (c) relatively poor infrastructure which can not attract foreign investment in the country.

The survey was conducted by BOI using a questionnaire, which were mailed to 59 companies registered with BOI (Joint-venture and 100% Japanese investment) and 14 Japanese companies registered in Chittagong Export Processing Zone (CEPZ). Out of the total **73**, answers were received from 18 firms registered with BOI and 8 firms in operation in Chittagong Export Processing Zone. The percentage of response was 35.6. Though the response was not significant yet in number it represents the views and opinions of the different Japanese firms operating in Bangladesh.

Moreover, two officers from BOI contacted directly 9 Japanese companies and agencies and interviewed the top management of firms to clarify and add to the findings of the mailed survey. The overall survey work was conducted between October to December 1996.

## **Major Findings of the Survey**

The study permeates that the Japanese companies were attracted to invest in Bangladesh mainly on grounds of low labour cost, facilities in EPZ with 10 years tax holiday and willingness of the people to work hard if opportunity is given. Most of the responding firms informed that they had an idea before coming that Bangladesh is a country of poverty, natural disaster and epidemic diseases. But the present impression by many firms towards Bangladesh represents a country of sufficiently enriched and having business potentials. However, certain issues entwine with the image problem of the country. Most important are political instability, repeated hartals and inefficient economy in built in red tapism. They pointed out about non availability of trained manpower, underdeveloped infrastructure, absence of any type of entertainment facilities for foreigners, small domestic market and meagre purchasing power as major impediments to attracting foreign investment. Many have also pointed out about discontinuance of policies/programmes committed by the previous government and unreliability in application of rules and regulations of the government. The major constraint/problems of investment identified from the survey are :-

- a. Political instability particularly repeated 'hartals' (strikes).
- b. Red tapism, bureaucratic hurdles and lengthy administrative procedures.
- c. Inadequate infrastructure particularly energy and telecommunication facilities.
- d. Traffic jam, indiscipline and disorder in city roads.
- e. Non availability of trained labour and managerial personnel.
- f. Limited local market and meagre purchasing power of the general people.

- g. High and irrational import duty for certain items.
- h. Complex tax system in the country in spite of introduction of reform measures.
- i. Contradiction of tax rates between description in rules and actual collection by the authority.
- j. Discontinuation of policies/programmes adopted by the previous Government(s).
- k. Low education level of the general people.
- l. Too many ministries/government agencies to deal with the same issue and corrupt practices such as graft.
- m. Harassment by the personnel from gas, telephone and municipal authorities.
- n. Rigid and *conservative banking* system and absence of service oriented banks.
- o. Lack of accurate information for taking correct business decisions.
- p. Poor reaction by authorities towards quick solution of the problems.
- q. Absence of entertainment facilities for the foreign investors.

The interviewed companies informed that during the implementation period they had faced problems of lack of accurate information related to investment, indecisive rules and regulation of the government, contradiction between what is written in the published document of the government and the actual procedure practised by the implementing agencies.

The foreign companies also faced problems during operation of their industries with having too many agencies to deal with the same



matter, complicated bank procedures, repeated power failure, unclear taxation system on imported materials, etc. They specifically pointed out that contradiction of tax rate between the description in Statutory Rules and Order (SRO) and the actual collection of tax by authorities (7.5% has been shown in the BOI guide book, but 30% actually imposed by custom authorities for imported machinery).

Certain companies also mentioned that due to non fulfilment of commitment by financial institutions they have to suspend implementation of their project. Delay in disbursing funds by the Bangladeshi financial institutions is also a factor for the slow progress of the projects. The responding companies informed that bureaucratic red tapism, poor reaction by authorities towards quick solution of problems and absence of stable economic situation hamper the flow of investment in the country.

The responding companies mentioned that, the bankers in Bangladesh are not at all service oriented. In most of the commercial banks, the bankers are very slow in action and delay in opening Letter of Credit and bill of collection. According to the investors, they are some times haughty, arrogant in dealing with clients. There is really short of service oriented banks, in the country. Certain Japanese company even complained about the high interest rate of the bank and very rigid and conservative banking system of the country. The responding companies also mentioned that most of the banks have no capacity for funding the international projects. In that case, they observed discrimination between a 100% foreign investment project to that of 100% locally owned company is inconsistent with the provision of equitable treatment for both foreign and domestic investors as mentioned in the BOI brochure.

The responding companies suggested for more investment by Bangladesh in backward linkage industries for supporting the technically developed industries. They felt that labour intensive and

infrastructure related projects, textile and garments, light industries, chemical industries, leather and leather goods, general machinery, civil construction work are the most promising sectors for foreign investment in Bangladesh.

The responding companies advised the foreign investors who may like to invest in Bangladesh for examining the pre-conditions before going for actual investment and compare investment climate in other neighbouring countries prior to taking investment decision. They also suggested the Japanese companies to hear from the Japanese firms already in business in Bangladesh and to be very much patient against slow movement in almost all aspects of business and investment. They also emphasized in selecting reliable local counterparts for their projects.

The companies further suggested to make BOI as a real workable 'one-stop investment service' institution for helping the foreign investors. They suggested BOI and Bangladesh Export Processing Zone Authority (BEPZA) to sort out the problems that the investors already in Bangladesh are facing and try to solve those immediately.

Most of the companies suggested setting up of a liaison office of BOI in major foreign countries including Japan for quick services to the investors and to organize business missions from major potential investing countries to observe market conditions in Bangladesh. They recommended for giving priority of posting of BOI officials in Tokyo and Osaka.

The responding firms agreed that general people of Bangladesh are friendly, helpful and gentle but lack sense of independence and absence of enterprising spirit. They are diligent, but lack sense of responsibility. They need acquisition of international views, vision and custom to work together with the foreigners. There are tremendous gaps in the society between the haves and have-nots.

## Recommendations for Improvement of **Investment Climate**

Following are the important recommendations for improvement of investment climate in Bangladesh:

- a. BOI backed up by the Bangladesh Embassy in Tokyo may consider to conduct aggressive propaganda and publicity through press, induction seminars/symposiums, advertisement in television and newspapers and magazines and participation in trade fairs to rebuild the image of the country. This includes publication and wide distribution of different types of promotional books including travellers guide among the potential investors.
- b. Improvement of basic infrastructure like uninterrupted supply of electricity, easily attainable telephone and gas line and water supply, both in quality and quantity. Review of outstanding laws and institution to be updated in observance of rules/decrees.
- c. Setting up of a liaison office of BOI in major cities like Tokyo and Osaka to provide appropriate and quick services to the Japanese investors, In this **regards** co-operation may be sought from the Chamber of Commerce and Industry of Tokyo and Osaka. BOI may also move for posting of its officials in the proposed overseas offices of local Bangladeshi Banks in Japan.
- d. Continuity of policies committed by the previous government review of rules and periodic.
- e. More investment in backward linkage industries should be encouraged for supporting technically developed industries.
- f. 'One-window service' or 'package services' facilities for the investors should be effectively introduced.

- g. Much effort and resources need to be put into human resource development and proper attention be given for upgrading the standard of education.
- h. Expedition and simplification of custom formalities for incoming and outgoing machines and products at Dhaka and Chittagong.
- i. Bangladesh currency 'Taka' should be made fully convertible.
- j. Bank service for handling of foreign exchange accounts of foreign companies and funding of foreign investment project must be made more efficient. Introducing of guidelines by the Government aimed at faster service in the banks through changing operational systems and improving staff efficiency. The responding companies recommended to change the official weekly holiday in Bangladesh from Friday to Sunday for the greater interest of boosting business and trade activities both locally and internationally.
- k. BOI of Bangladesh should study the competitive advantages of other countries, modify the incentives offered if needed and promote the advantages objectively along with the other aspects typical to Bangladesh.

Finally, as concluding remarks, many companies mentioned that the country needs to come to a general political consensus for ensuring uninterrupted production process in foreign and joint-venture companies. This is critical for attracting more Japanese investment in Bangladesh. Commitment from the Government by creating a congenial investment atmosphere and effective investment promotion drive by the investment promotion officials of the Government is a must for a successful investment promotion. Creation of facilities for comfortable living by the foreigners who stay longer in the country.

## Conclusion

The flow of Japanese investment started in late 1980s and continued upto early 1990's. But the trend of investment did not continue perhaps due to the three main reasons. First, the flood and cyclone of 1991 which affected many of the Japanese investments in Chittagong export Processing Zone. Secondly, frequent political disturbances created negative image of the country among the prospective investors in Japan. Thirdly, lack of adequate infrastructure facilities for attracting foreign investment. Due to these three main reasons, foreign investors particularly the Japanese investors were very shy in investing in Bangladesh. On the other hand, from early 1990's, China and Vietnam had opened their economy for foreign direct investment. Japanese companies had preferred investment in these countries for reasons of proximity, ethnic relations and also low labour costs. As low labour cost only cannot appeal to the Japanese investors for investment it is presumed that Bangladesh could be successful in attracting Japanese investment when the country would be politically stable and incentives offered to the foreign investors would be more competitive than other neighbouring countries. In addition, a well planned investment promotion strategy will also be required for an aggressive investment promotion drive to attract investment.

The Japanese industry is facing most serious turning point since bursting of the economic bubble, increased Yen appreciation and the ongoing recession. A shift to higher value-added production, entry into new business fields to enhance productivity and greater internationalization are important issues in its national agenda. On the other hand, Bangladesh has to put into place a comprehensive array of policies aimed at bringing about significant socio-economic

improvement to its people. In recognition of the private sector's ability to contribute towards achievement of the goals, the government has implemented a number of significant policy reforms. These are designed to create a more open and competitive climate for foreign investment and facilitate private sector initiatives. The present survey among Japanese investors would help Bangladesh to further improve its policy framework to attract foreign investors in the country. These together will offer a favourable environment for foreign investment in Bangladesh

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