UNIWERSYTET SZCZECIŃSKI
WYDZIAŁ NAUK EKONOMICZNYCH I ZARZĄDZANIA

Studia i Prace WNEIZ US
nr 53/2 2018

STUDIA I MATERIAŁY

DOI: 10.18276/sip.2018.53/2-23

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FOREIGN DIRECT INVESTMENT IN VIETNAM AFTER TEN YEARS OF WTO ACCESSION: TRENDS AND OPPORTUNITIES

Abstract

Foreign direct investment has been the key driver for Vietnam's economic development in recent years, especially after Vietnam joined the WTO in early 2007. By the end of 2016, FDI sector in Vietnam comprised for 25% total investment, 14.8% of state budget revenue, with total FDI accumulated of more than 293 billion USD. This paper analyzes some main features of FDI in Vietnam during the ten years period 2007–2016, after Vietnam's accession to the WTO. The author found that FDI in Vietnam has played an increasingly important role for the economic growth, especially in trade performance. However, FDI has been much focused on labor-intensive manufacturing and the linkages of FDI firms with domestic ones remain relatively weak. Based on this, the author suggests policy implications for attracting green FDI in the upcoming years.

Keywords: FDI, Vietnam, WTO accession, tax havens

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Introduction

In the context of integration, foreign direct investment (FDI) has played an important role for economic development, especially for emerging or transitional economies. Regarding to global investment trends, in 2015, global FDI flows jumped by 38% to 1.76 trillion USD, the highest level since the global economic and financial crisis of 2008-2009. Inward FDI flows to developed economies almost doubled to 962 billion USD, with a strong growth in Europe. Developing economies saw their FDI inflows reach a new high of 765 billion USD, 9% higher than in 2014. Developing Asia, with FDI inflows increasing by 16% to 541 billion USD, remained the largest FDI recipient in the world. The significant growth was driven by the strong performance of East and South Asian economies (UNCTAD, 2016). In this context, Vietnam has become one of the most favorable destinations for FDI attraction worldwide. In 2016, Vietnam ranked 6th in Asia and ranked 26th worldwide in terms of FDI inflows (UNCTAD, 2016). However, FDI in Vietnam experienced a high fluctuation in the last ten years. This paper finds out some main characteristics of FDI in Vietnam after joining the WTO, and gives some policy implications. The data used in this paper is based on the General Statistics Office of Vietnam and UNCTAD data, for the ten-year period from 2007–2016.

1. Materials and methods

With the low labor costs, strong openness to trade and an advantageous geographical location, Vietnam has been one of the most favorable destinations of FDI, especially after Vietnam's accession to the World Trade Organization in 2007. After one year joining the WTO, committed FDI reached a record high of 71.7 billion USD, 3.4 times higher than FDI committed in 2007 (Table 1). The main reasons for this surge were the wider investment opportunities, predictability and high responsibility for policy reforms in Vietnam after WTO accession. In the period 2009–2011, FDI registered declined dramatically, standing at 15.59 billion USD in 2011, which was the lowest level since 2007. It was caused mainly by the global financial crisis and some domestic factors such as the macroeconomic instabilities, power shortage and lack of skilled workforce. In a positive sign, despite the significant decline in FDI commitments, FDI implement saw a slight increase in the period 2009–2011, stood at 11 billion USD in 2011. Notably, foreign investors gradually shifted away from speculative real estate sector to manufacturing, resulted in an increase in employment and output (World Bank, 2016). In the period 2012–2016, committed FDI recovered significantly, from 16.3 billion USD in 2012 to 24.37 billion USD in 2016. FDI implements also experienced an upward trend, with an annual growth of 9.7% in this period. Up to the end of 2016, Vietnam attracted investments from 116 countries and territories, with total accumulated FDI commitments of 293.25 billion USD (equal to more than 150% of GDP). Only in 2016, there were 2556 new registered projects, with 24.37 billion USD of committed capital. In which, there were 1020 new projects in processing and manufacturing industry with total committed capital of 15.53 billion USD, accounting for 64% total investment capital, followed by electronic, fuel manufacturing and real estate, which comprised 11.6% and 7% of total FDI committed respectively.

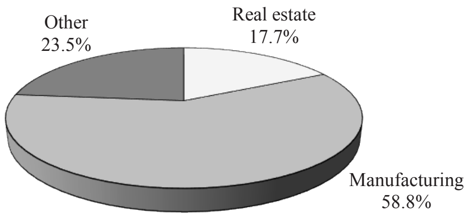
Table 1. FDI committed and FDI implemented in the period 2007–2016

Year	Number of Projects	FDI commitment	% change FDI commitment	% change FDI commitment	FDI implement
		(millions of USD)	(2007 = 100)	(previous year = 100)	(millions of USD)
2007	1544	21,348.8	100.0	–	8,034.1
2008	1171	71,726.8	336.0	336.0	11,500.2
2009	1208	23,107.5	108.2	32.2	10,000.5
2010	1237	19,886.8	93.2	86.1	11,000.3
2011	1186	15,598.1	73.1	78.4	11,000.1
2012	1287	16,348.1	76.6	104.8	10,046.6
2013	1530	22,352.2	104.7	136.7	11,500.0
2014	1843	21,921.7	102.7	98.1	12,500.0
2015	2120	24,115.1	113.0	110.0	14,500.0
2016	2556	24,372.1	114.2	101.1	15,800.1

Source: *General Statistics Office of Vietnam*.

Regarding to FDI by sectors, most of FDI in Vietnam has gone to labor intensive manufacturing, accounting for 58.8% of all FDI inflows in the period 2007–2016. As a result, Vietnam has emerged as global manufacturing and assembly hub, integrated into global supply chains. Most investments are focused on light industries such as computers, mobile phones and electronics. Especially, an increasing number of high technology through nations companies (TNCs) such as Samsung, Intel, Microsoft, Rockwell Automation… has invested and decided to expand operation in Vietnam (only Samsung has pledged up to more than 12 billion USD of investment to the end of 2015, with 3 projects in Bac Ninh, Thai Nguyen and Ho Chi Minh city). Besides manufacturing, the second-biggest recipient of FDI in Vietnam was the real estate sector, comprising for 17.7% of the total committed FDI in the period 2007–2016. It is notably that the high rate of investment in real estate construction sectors stimulated by the property market bubble has contributed to macroeconomic instability (Nga. T.N, 2011). In the "bubble period" from 2008–2011, nearly 50% of total FDI in Vietnam was invested in real estate sector, and the rate for 2016 was only 7%. The FDI movement from the speculative sectors like real estate to labor-intensive manufacturing sector is expected to be continued in the period 2016–2020 due to the orientation of the Vietnamese government.

Figure 1. FDI by sector in the period 2007–2016

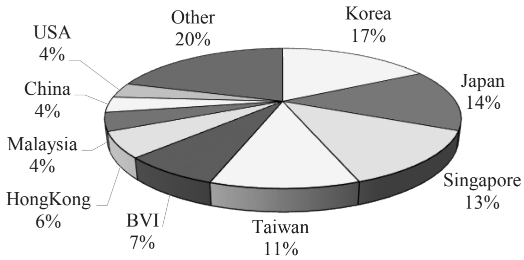


Source: *General Statistics Office of Vietnam.*

Regarding to FDI by sources, regional investors are the most active in Vietnam. Despite Vietnam is the host country for 116 countries and territories worldwide, the majority of FDI in Vietnam has come from East Asia, in which Korea, Japan, Hong Kong, Taiwan accounting for nearly half (48.2%) of total FDI registered. ASEAN countries constituted around 20% of the FDI inflows. In which, Singapore (12.9%) and Malaysia (4.2%) are the two most active investors. However, FDI from the United States and Europe are moderate, only comprising less than 10% of the total FDI commitment. Notably, in the last three years (2014–2016), Korean investors were the most active one in Vietnam with 7.7 billion USD registered in 2014, 6.98 billion USD in 2015 and 7.04 billion USD in 2016, accounting for 35.1%, 28.9% and 29% of the total committed FDI respectively (FIA, 2017). The gradual movement from investors from China, Taiwan, Malaysia in the "bubble period"

2008–2011 to investors from Korea, Japan, Hong Kong and Singapore in the period 2012–2016 was an encouraging sign, which puts Vietnam to a higher level of the global value chains.

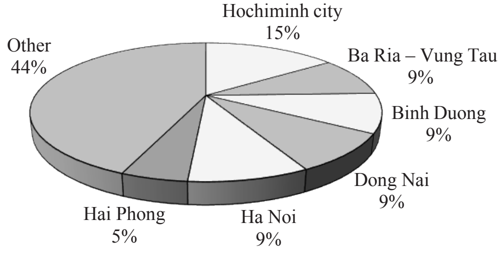
Figure 2. FDI by countries and territories in the period 2007–2016



Source: *General Statistics Office of Vietnam.*

Regarding to FDI by regions, most of FDI has come to the South of Vietnam. In which, Ho Chi Minh City is the largest FDI recipient, accounting for 15.3% of total FDI commitment, followed by Ba Ria Vung Tau (9.2%), Binh Duong (9.1%) and Dong Nai (8.8%). Notably, in recent years, there has been a surge in FDI to the North of Vietnam, especially in Bac Ninh, Thai Nguyen and Hai Phong. However, there are a large number of provinces (34/63) which have FDI stock comprised for less than 0.5% of total FDI committed. Especially, in 2016, 16 of 63 provinces had no new FDI projects. It means that many provinces in Vietnam are not active in attracting FDI, and still much rely on investment from the state budget.

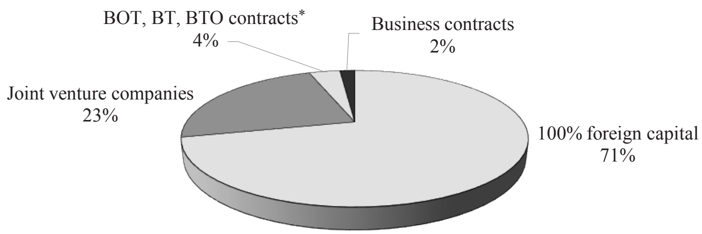
Figure 3. FDI by regions in the period 2007–2016



Source: *General Statistics Office of Vietnam.*

Regarding to FDI by forms, Most FDI in Vietnam are green field investments that are fully owned and operated by foreign investors. Foreign investors have overwhelmingly chosen to invest via 100% foreign-owned enterprises – currently accounting for 71.4% of all Vietnamese FDI projects. The high rate of 100% foreign FDI firms goes with a low level of knowledge and technology transfer. Vietnamese government encourages joint venture firms with horizontal FDI, to take the advantages of spillover effect of FDI firms for the domestic market. However, most of FDI so far (60%) is vertical FDI, mainly focus on labor- intensive production, with moderate level of value added. The imbalance of FDI by forms has raised the question of the role of FDI in transferring knowledge and technology for the domestic market.

Figure 4. FDI by forms in the period 2007–2016



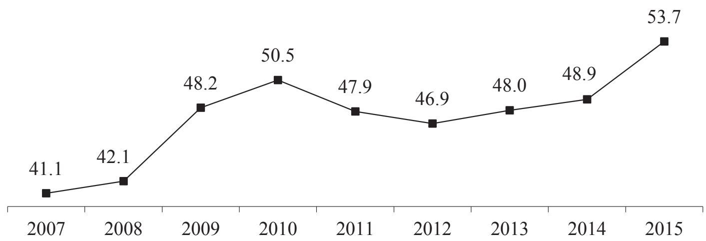
* BOT: Build–operate–transfer; BT: Build–transfer; BTO: Build–transfer–operate.

Source: *General Statistics Office of Vietnam.*

2. Results

FDI in Vietnam saw a big surge after the accession to the WTO. As a result, FDI sector has been a main engine for Vietnam's economic development. By the end of 2016, FDI firms created 3.9 million jobs, or 7% of the labor force. FDI sector also comprised for more than 20% of GDP and 25% of total investment in the period 2011–2016. The contribution of FDI for state budget has increased, reached 14.4% in 2015, almost double 7.4% in 2005. Based on UNCTAD data, the FDI stock represented, on average, 47.5% of GDP during the period 2007–2015. In 2015, the FDI stock exceeded 50% of GDP, stood at 53.7% (Figure 5). With a high level of integration to the global economy, it is expected that FDI will have stronger contribution for the economic growth of Vietnam in the upcoming years.

Figure 5. FDI stock as a percentage of GDP in Vietnam in the period 2007–2015 (%)

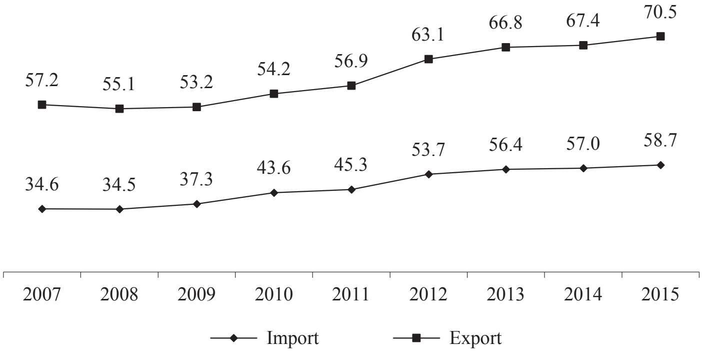


Source: *own calculation based on UNCTAD data.*

FDI firms have, especially, played an increasing important role for trade performance. The contribution of FDI sector in Vietnam's total imports/exports remarkably increased (Figure 6). Since 2007, the majority of Vietnam's total exports and imports were implemented by FDI sector. In 2015, the FDI sector accounted for 70.5% of Vietnam's total export, with a 25% growth over the last decade. With export-oriented manufacturing FDI sector, Vietnam's export composition has shifted from agricultural and primary commodities to labor-intensive manufacturing and hi-tech goods. FDI firms are the key exporters in smart phones (100%), electronics and computers (97%), vehicles and parts (93%), footwear (81%), luggage and bags (80%) and garment (60%) (World Bank, 2016). FDI sector also has boosted import activities, especially for machinery and equipment. In 2015, FDI sector comprised 58.7% of Vietnam's total import. The strong export surplus of FDI sector has helped Vietnam to mitigate its trade deficit as well as contribute to Vietnam's macroeconomic stability.

However, FDI in Vietnam after WTO accession has experienced some difficulties. Many issues such as polluted environment, imbalance of FDI by sectors, imbalance of FDI by regions, lack of human resources, especially skilled workforce remain the "bottle necks" for FDI attraction in Vietnam. Besides these traditional issues, this paper focuses on analyzing two recent trends may negatively affect the sustainable of FDI in Vietnam.

Figure 6. Share of FDI in Vietnam's exports–imports (%)



Source: *General Statistics Office of Vietnam.*

Firstly, the spillover effect of FDI firms on domestic firms as suppliers remain relatively weak. On the other hand, there are domestic firms which are largely inward oriented and serving the domestic market. The linkages between these two segments are very limited. As such, the FDI sector operates in isolation rather than serving as a broader catalyst for growth, with limited spillovers to the domestic private sector in the form of increased demand for inputs, access to new technology and managerial techniques, demonstration effects and agglomeration benefits. The expanding labor-intensive manufacturing sector has not stimulated the development of supplier industries such as cotton and synthetic cloth, dyes, chemicals, plastics and steel. As the experience of Japan, Korea, Taiwan (China), Singapore, and now China shows, export value added can be enhanced through heightened technological intensity in exported products and services. These examples also show that an export model that is primarily based on low labor cost and labor intensive, low technology exports will ultimately diminish as wages inevitably rise (WB, 2016).

Secondly, there are an increasing number of FDI invested in Vietnam from tax-havens. In the last six years (2011–2016), there was a strong rise in FDI from countries and territories known as the 'tax havens' such as British Virgin Islands, Singapore, Hong Kong, Cayman, Bermuda, Panama, Jersey, Luxembourg, New Zealand, Bahamas, Panama, Delaware State in the US, Switzerland, and Ireland. In which, only Singapore, BVI and Hong Kong comprised for 26% of total FDI stock. Increasing of FDI from tax havens has raised the question about tax lost, which remains a controversial issue in Vietnam.

3. Discussion

FDI has been a main engine for economic growth in Vietnam after the WTO accession. The increasing role of FDI in Vietnam is inevitable. However, to avoid the negative effects of FDI and towards sustainable or “green” FDI, the Vietnamese government should focus on solving the “bottle necks” on attracting FDI as well as reject unsuitable FDI projects.

First, Vietnam should strengthen the linkages between domestic and FDI enterprises. One of the basic solutions is paving the way for the development of supporting industries. At present, the supporting industries only meet about 30% of the demand of FDI enterprises, creating a large import pressure and reducing the linkage of domestic and FDI enterprises. Moreover, the development of supporting industries will also play an important role in helping Vietnam more integrated to the global value chain. Currently, there are only 21% of Viet Nam enterprises getting involved in the global supply chain, compared to Thailand (30%), and Malaysia (46%). So, Vietnam should complete many tasks to strengthen the integration of domestic goods and service suppliers.

Second, Vietnam should attract selective FDI which has high value-added, advanced technology and environmental friendliness. Vietnam needs to attract good investors, especially multinational corporations which have high level of corporate social responsibility. To do this, it is necessary to fulfill the legal system and policies related to investment, which must be consistent, transparent, predictable and competitive with other countries. Furthermore, Vietnam should complete mechanisms and policies for attracting hi-tech and environmental friendly projects; issue standards to limit and prevent FDI projects with low quality.

Third, Vietnam should be better in planning in many levels including general planning, sector planning and regional planning. The Ministry of Planning and Investment will coordinate with relative ministries and localities to propose comprehensive solutions to ensure the implementation of these plans, such as: infrastructure investment, electricity supply, material and human resources supply etc. Well organized planning will pave the way to attract worth FDI projects, suitable with the orientation of Vietnamese government.

Forth, it is crucial to implement investment promotion through investment funds, banks, financial companies, law firms, foreign consulting companies etc. These financial institutions are important partners which can strongly affect the investment decision of foreign investors. Besides, it should be focus on on-site investment promotion through solving the difficulties of existing investors. Particularly, investment promotion should focus on attracting good quality FDI projects which achieve the goal of sustainable economic development; eliminate the projects which have potential environmental damage and backward technology.

Fifth, it is necessary to improve the quality of human resources. In the context of integration, FDI inflows are likely to increase sharply in the coming time, which put a higher pressure on human resources demand, especially skilled workforce. To welcome the flow of FDI in the context of the 4.0 industrial revolution, it is necessary to maximize effectiveness of the golden population structure and strengthen linkages between enterprises and training institutions. It can make businesses quickly recruit suitable employees, reduce training and re-training cost. Particularly, it is crucial to improve the quality of human resource demand forecasting. Reliable forecasting can help to reduce the cost of re-training as well as avoid wasting social resources.

Conclusions

Vietnam is one of the most dynamic and fast-growing economies in the Asia Pacific region. Vietnam also has joined a wide range of free trade agreements such as Vietnam–Korea, Vietnam–EU, the ASEAN economic community (AEC) and RCEP etc. In this context, FDI into Vietnam is expected to increase rapidly with the rate of 10–15% annually over the next five years. After ten years of WTO accession, FDI has played an important role for economic growth, job creation and trade balance improvement. However, the issues of transfer pricing, tax evasion and sector imbalance are limitations need to be solved in the coming years. To enhance FDI attraction while maintain macro economy balance, the Vietnamese government should issue policies to attract green, high-tech FDI and more active in investment promotion. Particularly, it is crucial to strengthen the linkage between domestic enterprises and FDI enterprises to integrate deeper in the global value chain.

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BEZPOŚREDNIE INWESTYCJE ZAGRANICZNE W WIETNAMIE PO 10 LATACH OD AKCESJI DO WTO. TENDENCJE I SZANSE

Streszczenie

Bezpośrednie inwestycje zagraniczne są w ostatnich latach podstawowym czynnikiem rozwoju ekonomicznego Wietnamu. Uwidoczniło się to szczególnie po przystąpieniu Wietnamu do WTO na początku 2007 roku. Na koniec 2016 roku BIZ stanowiły 25%

łącznych inwestycji Wietnamu, 14,8% wpływów budżetowych. Ich skumulowana wartość wynosiła ponad 293 mld USD. W opracowaniu analizowano główne cechy BIZ w Wietnamie w latach 2007–2016, po przystąpieniu Wietnamu do WTO. Wyniki badań wskazują, że BIZ stanowią ważną i rosnącą rolę w rozwoju ekonomicznym kraju, szczególnie w sektorze handlu. BIZ skoncentrowane są jednak w wysoce pracochłonnych gałęziach przemysłu przetwórczego i związki z krajowym przemysłem są względnie słabe. Autor sugeruje zatem realizację polityki przyciągania „proekologicznych BIZ".

Słowa kluczowe: BIZ, przystąpienie do WTO, raje podatkowe

Kody JEL: F21, F23