Foreign Direct Investment in Vietnam: Achievements and Challenges

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■ Foundation for FDI in Vietnam

- Before 1986, Vietnam was characterised as a centrally planned economy which did not encourage private sector and foreign direct investment (FDI). However, since the implementation of Doi Moi Reform in 1986 which started the country' s economic liberalization, cooperation in investment with foreign countries in order to take advantage of capital, technology, management skills and export markets to facilitate the industrialization and modernization process of the country has been determined to be an important strategy for Vietnam. The Law on Foreign Investment of Vietnam first promulgated in 1987 provided the legal framework for FDI in the country. Since then the Law has been amended and supplemented several times. The latest version of the Law regulating FDI in Vietnam is the Law on Investment which came into effect from July 2006. Vietnam also passed some legal documents which stipulate detailed guidelines for the implementation of the Law.

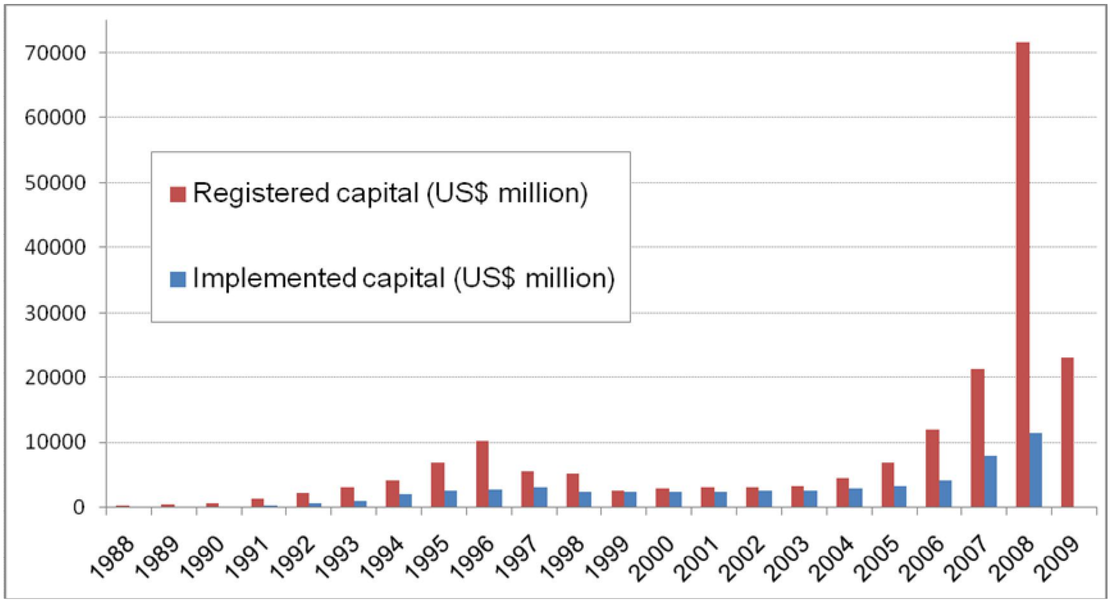
■ Vietnam' s FDI statistics[1]

- Over the past 25 years, Vietnam has created an impressive story in attracting FDI. The inflows of FDI into Vietnam generally keep increasing over the past two decades. According to the data of the General Statistics Office of Vietnam (GSO), registered FDI increased from US$347.1 million to US$23.1 billion in 2009 with the implemented capital of US$10 billion. During the same period, the number of licensed foreign investment projects rose from 37 to 1,208. The country witnessed considerably

[1] General Statistics Office of Vietnam (GSO) and Foreign Investment Agency (FIA)

decrease in registered FDI during 1997-2000 and from 2008 due to the regional and global financial crises occurred in 1997 and 2008, respectively. The implemented capital, however, is quite stable with about US$10-11 billion/year. By February 2012, Vietnam had 13,530 valid FDI projects with the total accumulated registered capital of US$199.7 billions and the implemented amount of over US$80 billion.

Figure 1 – FDI flows into Vietnam during 1988-2009



(*) Include the increase amount of existing licensed projects
Source: General Statistics Office of Vietnam (*GSO)*

- Currently, there are 95 countries and territories that have made investment in Vietnam. The top five investors in terms of registered capital include Japan (12.38%), Singapore (12.06%), South Korea (11.98%), Taiwan (11.81%) and British Virgin Islands (7.51%). These five countries and territories account for 55.74% of the total registered capital of Vietnam.
- Geographically, FDI projects are allocated to most provinces and cities of the country. The majority share flows into Ho Chi Minh City, Ba Ria - Vung Tau, Hanoi, Dong Nai and Binh Duong, which are key economic areas with more developed infrastructure, abundant labor force and other favorable investment environment. These five areas have attracted about 57.7% of the total pledged capital and 9,756 FDI projects in Vietnam.
- The two main forms of FDI selected by foreign investors in Vietnam are

wholly-owned foreign enterprise and joint venture with the registered capital of US$183 billion, equal to 91.8% of the total capital, and 13,103 projects or 96.8% of the total number of FDI projects in the country. Concerning FDI by field, the lion share of FDI flows into 5 main sectors including manufacturing, real estate, construction, accommodation and food services, and electricity-gas-steam-water supply. These five sectors account for 86.79% of the total accumulated registered capital (US$171.78 billion) and 9,581 projects.

Table 1 –FDI structure in Vietnam by 2011

Order	Industry	No. of projects	Registered capital (USD)
1	Manufacturing	7,987	93.053.036.629
2	Real estate	373	47.002.093.570
3	Construction	839	12.499.828.279
4	Accommodation and food services	314	11.830.450.512
5	Electricity, gas, steam and water supply	68	7.397.576.933

Source: Foreign Investment Agency (*FIA)*

- After 25 years, FDI sector has now contributed about 19% to Vietnam' s GDP, US$3.5 billions to the government' s budget, accounted for 59% of the country' s total exports excluding crude oil and created 2 million job opportunities for Vietnamese workers. This sector also has positive impact on the economic structure of Vietnam. If the ratio of agriculture in GDP in 1988 was 80%, it shrank to about 22% in 2011. Industry and service now account for 78% of the country' s GDP. Therefore, it is needless to say that FDI has played an important role in the development of Vietnam.

■ Challenges for Vietnam in attracting FDI

- The achievements of Vietnam in attracting FDI are clearly attributed to the country' s efforts in improving its investment environment like maintaining socio-political stability, perfecting the legal system, improving infrastructure, creating 234 industrial zones and export processing zones, high-tech and economic zones with many incentives for foreign investors and many other activities in promoting FDI. However, to maintain the country as an attractive destination for FDI, there are still works for Vietnam to do.

– Firstly, even though it has been upgraded in recent years, the infrastructure of Vietnam fails to meet the needs for economic development because the economy grows too fast. According to the World Economic Forum, infrastructure of Vietnam was ranked 123 out of 142 investigated countries in 2011. The position of road and port systems of the country were 123 and 111, respectively. Rank above 90 denotes disadvantage for the country.

Table 2 – Quality of infrastructure global ranking of Vietnam

Infrastructure	Rank / 142
Quality of overall infastructure	123
Quality of roads	123
Quality of railroad infrastructure	71
Quality of port infrastructure	111
Quality of airport infrastructure	95
Available airline seat kms/week, millions	34
Quality of electricity supply	109
Fixed telephone lines/100 pop	70
Mobile telephone substription/100 pop	5

Source: The Global Competitiveness Report 2011-2012.

– The second challenge to Vietnam relates to human resource. Cheap and abundant labor force was once considered as a strength of Vietnam in attracting FDI. Recently, however, the country faces the competition from other countries like Indonesia and Myanmar in this respect. In addition, the quality of labor force is also a concern for Vietnam as well as foreign investors. According to GSO, Vietnam has the population of 87 million people, the majority of which, 62 million (more than 70%) are farmers. Workers account for 9.5 million (approximately 10%) while the number of intellectuals are about 2.5 million or 2.15% of the total population. The quality of the labor force is not high due to the shortage of skilled workers. 32% of foreign investors in a recent study of FIA and United Nations Industrial Development Organization (UNIDO) responded that their firms were unable to run at full capacity due to the lack of high-tech workers.

- Furthermore, it is necessary for Vietnam to develop its supporting industry to supply inputs for other industries, especially manufacturing. Having an effective and strong supporting industry not only increases the value added created in Vietnam in the value chain and the competitiveness of Vietnam's industry as a whole but also is an important factor attracting FDI. Vietnam, however, has a weak supporting industry in terms of both quantity and quality. There are a few domestic firms producing parts and components that meet the demands of foreign investors regarding design and quality. As a result, foreign invested firms have to import a large amount of inputs for their operation. This leads to an increase in production costs, reducing the competitiveness of these firms. Vietnam's garment and textile industry, for example, is ranked among the top 5 in the world but depends heavily on imported materials. According to GSO, the exports of this industry in 2010 reached US$11.2 billions, increasing 23% compared to that of 2009. However, the imports of this industry was up to US$5.3 billion.
- Despite Vietnam has made great efforts in perfecting its legal system for investment, in general, and for foreign direct investment, in particular, over the past 25 years, the current laws regulating foreign investment still contain unclear points and overlapped legal documents, leading to different interpretations in the application process. Other problems such as high inflation, administrative procedures, protection of intellectual property rights and corruption also raise concerns for foreign investors.

■ Prospect for FDI in Vietnam

- Even though there is a decrease in FDI commitment in Vietnam in recent years due to the impact of the global financial crisis and the speed of improving business environment in Vietnam does not satisfy the demand of foreign investors, there are still signs for a bright prospect for FDI in the country. The FDI disbursement in Vietnam is quite stable, standing at US$10-11 billion annually. Many investors show their interests in Vietnam's growing consumer market, young labor force, political and social stability, and see investment opportunities in the country. According to the World Investment Report 2012 of the United Nations Conference on Trade and Development (UNCTAD), Vietnam was ranked 11th among the most prospective host countries for FDI for the period 2012-2014. In the long-run, there is no doubt that Vietnam needs to find effective solutions to address its weaknesses regarding business environment in order to maintain the country’ s attractiveness to foreign investors.

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