EVFTA: OPPORTUNITIES AND CHALLENGES TO ATTRACT EU FOREIGN DIRECT INVESTMENT FLOWS TO VIETNAM

Dr. Nguyen Thi Thanh Mai
Swinburne Vietnam, FPT University
Email: maintt50@fe.edu.vn

1. Introduction

Since commencing the Renovation ("Đổi mới") process, Vietnam has actively participated in a number of multilateral, regional, and bilateral free trade agreements (FTAs). Thus far, 15 FTAs have been signed and ratified, and two more are under negotiation. The Free Trade Agreement between Vietnam and the EU (EVFTA) is a new-generation FTA, expected to improve Vietnam's attractiveness to foreign investors significantly. EVFTA is considered the most ambitious agreement that Vietnam has ever joined, and also the FTA with the highest level and scope of commitment that the EU has ever signed with a developing country. Therefore, the implementation of EVFTA will bring many opportunities for the EU's Foreign Direct Investment (FDI) flows to Vietnam. However, this agreement also poses multifold challenges for Vietnam amid the gloomy and uncertain context of the world and EU economy recently. This article aims to analyze the EU's FDI status in Vietnam, identify opportunities and challenges of the EVFTA, and then propose some solutions for the Vietnamese government to attract high-quality FDI inflows from the EU, which is in line with the country's development goals..

2. Overview of EU's FDI flow to Vietnam

Since the official establishment of diplomatic relations in 1990, EU's FDI into Vietnam has tended to increase, but the scale of capital flows is generally small, unstable, and significantly affected by the global and the EU economic fluctuations **(Figure 1).** Despite being a prominent outward foreign direct investor, the EU's FDI to Vietnam is minimal, barely accounting for approximately 3-5% of Vietnam's total FDI from 2010-2021. By the end of 2022, the total EU's registered FDI in Vietnam is nearly USD 27.9 billion, making up 6.36% of the total FDI in Vietnam (Ministry of Planning and Investment, 2022). In addition, EU projects entering Vietnam are usually of small average value, from 1 million USD to less than 7 million USD.

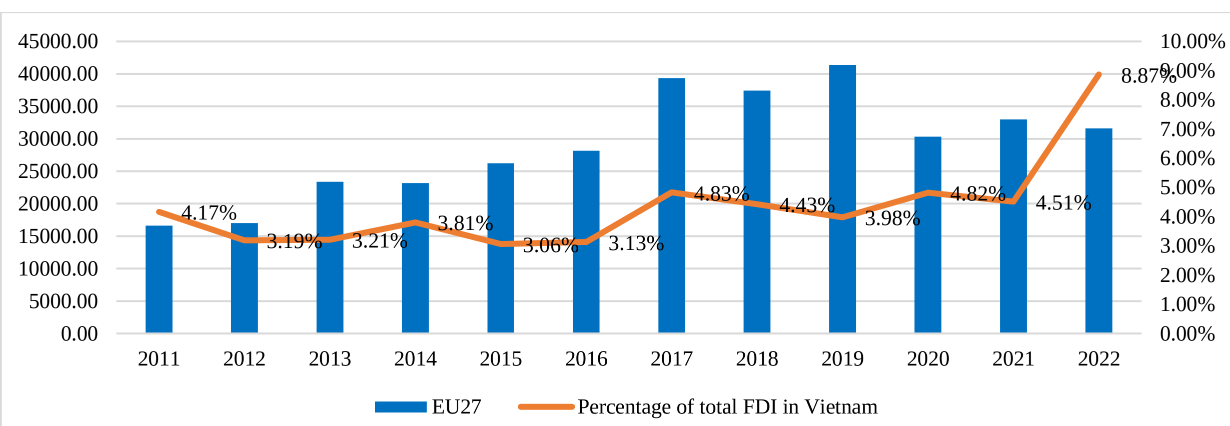


Figure 1. Total newly-registered EU FDI in Vietnam and share of total FDI

Source: Compiled from the Ministry of Planning and Investment (2011-2022)

By the end of 2022, the total registered capital of EU's 27 members is only ranked 6th among the leading investment partners of Vietnam, after South Korea, Singapore, Japan, Taiwan, and Hong Kong (**Figure 2**). Likewise, the investment capital scale into Vietnam accounts for only a minimal amount of the EU's total outward FDI, ranging from roughly 2 to 4% in the period 2013-2018 (EU-ASEAN Business Council, 2019); in 2019-2021, this figure is only approximately 0.23-0.35% (eurostat, 2022).

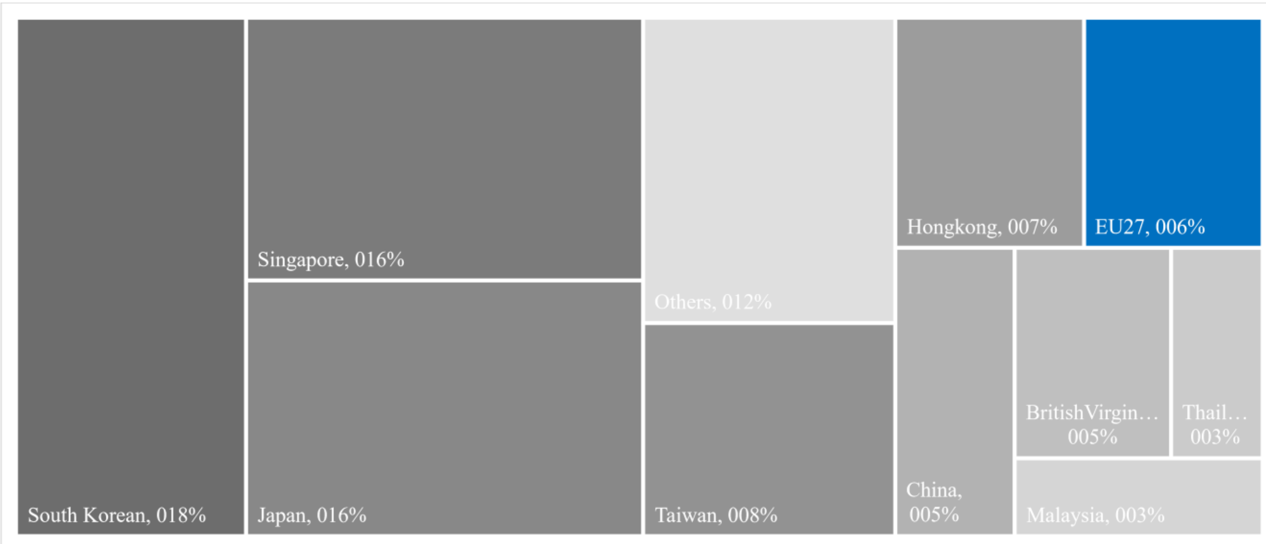
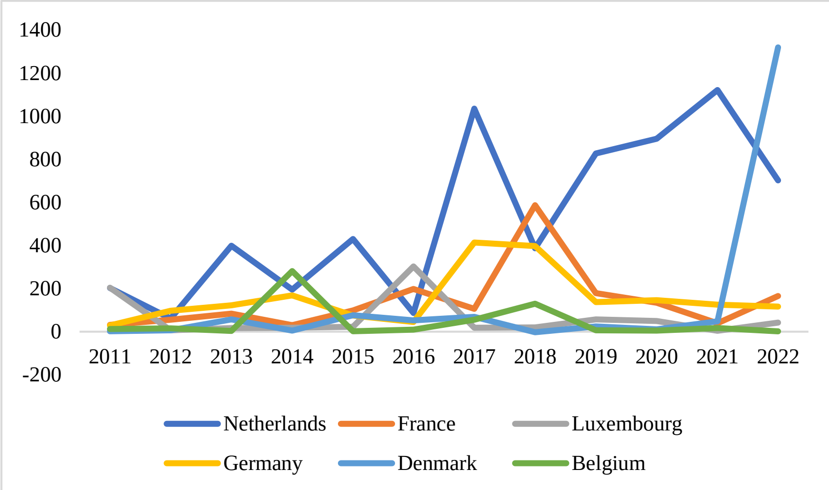


Figure 2. Total registered investment capital (million dollars) in Vietnam by partners, accumulated by the end of 2022

Source: Calculation based on data from the Ministry of Planning and Investment (2022)

Among the member states, six investors, including the Netherlands, France, Luxembourg, Germany, Denmark, and Belgium, account for more than 91% of the total EU's FDI into Vietnam, and only the Netherlands is in Vietnam's top 10 largest investors. Accumulated to the end of 2022, the number of Dutch projects is 410, with a total registered capital of USD 13.7 billion, accounting for nearly 50% of the total EU capital in Vietnam. Second is France, with 660 projects and USD 3.76 billion. Next is Luxembourg (61 projects and USD 2.62 billion); Germany (441 projects and USD 2.37 billion); Denmark (155 projects and USD 1.79 billion), and Belgium (82 projects and USD 1.1 billion). Other EU partners have invested in Vietnam, with a total accumulated registered capital of under USD 500 million, accounting for a negligible proportion **(Figure 3).**

Investment by EU enterprises in Vietnam is concentrated in the manufacturing industry, which is different from the general trend in the ASEAN region. In ASEAN, EU enterprises invest the most in the financial and insurance sectors, followed by the processing and manufacturing industries; wholesale, retail, and repair of automobiles, motorcycles, and other motor vehicles; information and communication **(Figure 4)** (ASEAN Stats, 2022). Meanwhile, in Vietnam, EU investors are most interested in manufacturing, electricity production and distribution, and real estate business. In 2021, the number of projects in the manufacturing sector was 608, registered capital of 8.43 billion USD (accounting for 37.92% of the total EU's FDI capital), followed by the electricity distribution production sector with 28 projects and USD 4.8 billion (21.6%), and the real estate business with a capital of 1.8 billion USD (8.2%).



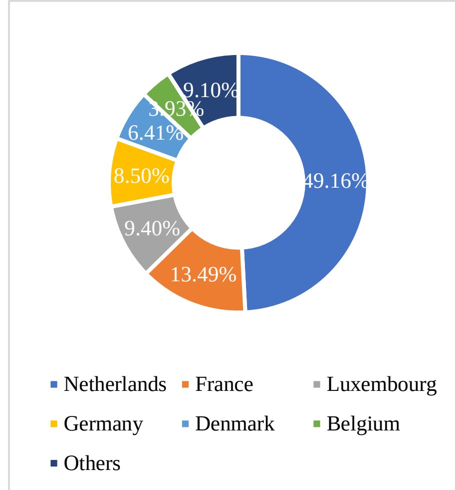
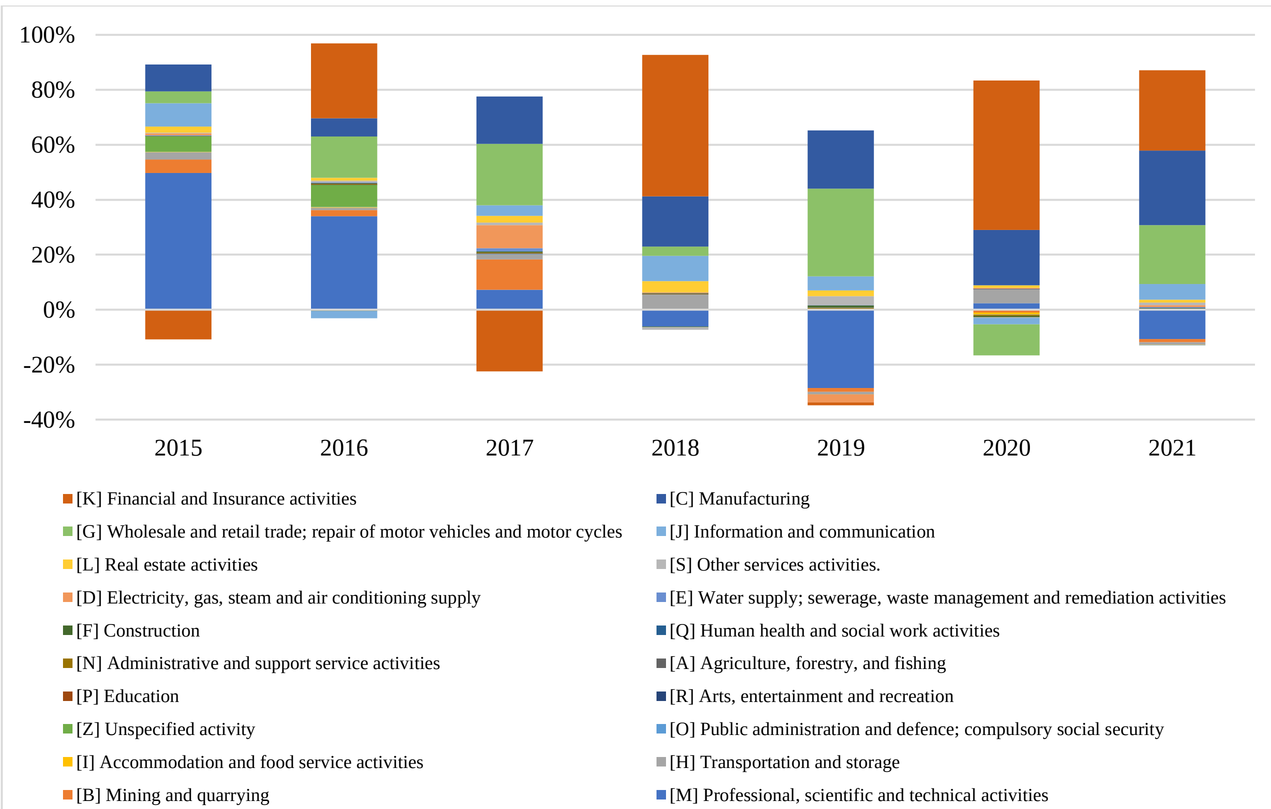


Figure 3. Registered capital for the period 2011 – 2022 and accumulated capital by 2022 of six major EU partners entering Vietnam (unit: million USD, %)

Source: Compiled based on data from the Ministry of Planning and Investment



Note: The negative weight is because the capital withdrawn is larger than the new investment

Figure 4. EU-27 FDI into ASEAN by sector (2015-2021)

Source: Reproduced from ASEAN Stats data (2022)

Considering the case of German investors as a prime example. Currently, 83 German enterprises (accounting for 20.8% of German enterprises in Vietnam) are investing in the manufacturing sector (Koslowski, 2022). Although Germany is a country of cars and machines, most businesses investing in Vietnam are in the garment sector, with large investors like Hugo Boss or Trigema. In addition, 18 companies in the chemical sector are investing in Vietnam, mainly to serve the domestic market. Messer Gases is the largest enterprise in this field, with a total investment capital of USD 228 million. As for the auto industry, although Vietnam does not have sufficient local suppliers to collaborate with German enterprises; however, Schaeffler, Bosch, and Mercedes-Benz have started investing in the country (Koslowski, 2022). Bosch is Germany's largest investor in the automotive sector, with a total investment of USD 350 million - with a sizeable belt-manufacturing complex in Dong Nai and an R&D center in Ho Chi Minh City.

Figure 4. The largest German investors in the manufacturing sector in Vietnam

Source: Koslowski (2022)

Recent trends have shown that EU businesses are increasingly interested in service sectors in Vietnam, such as logistics, post and telecommunications, finance, offices for rent, retail, supporting industries, food processing, and high-tech agriculture. EU enterprises have also been interested in investing in the nearshore and offshore wind power sector, such as CIP Group (Denmark), Orsted Group (Denmark), National Energy Group of Norway - Equinor, PNE Group (Germany), Pondera Company (Netherlands), EAB Company (Germany), etc. Some businesses have invested in the solar energy sector, such as EDF Renewables (France), Oil and Gas Group Total (France), etc.

3. Opportunities and challenges of Vietnam in attracting EU's FDI in the context of EVFTA implementation

The EVFTA is a comprehensive and high-quality agreement with a broad scope and high level of commitments, ensuring a balance of interests for both Vietnam and the EU while considering the difference in development levels between the two sides, thereby strongly affirming the desire and determination to create breakthroughs in upgrading the Vietnam-EU trade and investment relations, and at the same time contribute to strengthening the EU's presence in the Asian market. FDI often follows strong trade relations. On the other hand, abundant FDI inflows further promote the potential of trade between partners.

The signing and implementation of the EVFTA bring Vietnam various opportunities to attract the EU's FDI. *First*, the early signing of an FTA with the EU will create a competitive advantage for Vietnam over neighboring countries with similar economic structures, such as Thailand, Indonesia, Malaysia, or the Philippines. However, this advantage may be short-term, as ASEAN and the EU have launched the negotiation toward an interregional FTA. *Second*, the tariff elimination commitments within the EVFTA framework allow Vietnam to attract more EU's FDI since EU businesses will expand their investment to Vietnam to take advantage of these incentives. At the same time, they will have the opportunity to access the dynamic and large-scale ASEAN market. *Third*, commitments to trade in services and investment will also create opportunities to increase the EU's FDI inflows into Vietnam because the EVFTA has broader and deeper market access commitments than WTO. Since EU members are highly competitive in finance and telecommunications, improving market access will lead to a wave of investment in these two services. *Fourth*, the EVFTA implementation will be Vietnam's driving force and the requirement to reform its institutions and legal framework, improving the business environment and creating more favorable and safe investment conditions for investors.

However, the EVFTA implementation also pose some challenges to attracting FDI from the EU into Vietnam. *First*, the EVFTA is one of the conditions to attract EU investors; risks from the new context may weaken the business sentiment of EU investors. The EU economy is facing the problem of slow economic growth due to the adverse and long-term effects of the financial crisis since 2008; Europe's public debt crisis since 2009, unemployment, issues from intra-regional differences, migration, Brexit, Covid-19, the Russian-Ukrainian war, etc. Unstable matters in the world economy, such as inflation, food security, energy security, unemployment, populist movements, protectionist trends, climate change, natural disasters, etc., will increase investment uncertainty and slow FDI inflows from the EU. *Second*, new-generation FTAs such as the EVFTA pose significant challenges requiring Vietnam to perfect institutions, policies, and laws to ensure consistency, synchronization, fairness, transparency, non-discrimination, proper treatment, and procedures to limit disputes arising with foreign investors and effectively resolve these disputes. EVFTA requires higher investment in publicity, transparency, intellectual property rights, labor and human rights, and anti-corruption. *Third*, Vietnam's business environment still has many areas for improvement, such as low institutional quality, limited policies to attract FDI, low infrastructure quality, and human resources quality. These are major obstacles for Vietnam in attracting high-quality FDI inflows to Vietnam.

In order to take advantage of the opportunities and limit the challenges of the EVFTA in attracting EU’s FDI flows to Vietnam, a number of solutions need to be implemented. *First*, reforming institutional quality, where the government needs to develop a sustainable and predictable regulatory framework. *Second*, improve the quality of the business investment environment. *Third*, to complete different types of investment facilitation and consulting services. *Four*, continue to improve the quality of human resources and infrastructure.

4. Conclusion

Vietnam is actively participating in the process of globalization and international economic integration. In that integration trend, FDI has been and will continue to be an important source of investment capital for Vietnam's economic growth and development. Among different partners, Vietnam needs to focus on attracting FDI from the EU - a prominent international alliance with specific influences in Asia. After 35 years of cooperation in the field of investment, the EU's FDI in Vietnam is showing more positive signs in quantity and quality, contributing to remarkable changes in the country's socio-economic development. However, compared with the positive relationship between Vietnam and the EU, this capital flow still needs to be commensurate with the two sides' potential and expectations. To continue attracting high-quality FDI inflows in the coming time, the Government needs solutions to improve institutional quality, business investment environment, and appropriate policies. It is necessary to continue improving human resources and infrastructure quality.

LIST OF REFERENCES

ASEAN Stats. (2022). *Flows of Inward Foreign Direct Investment (FDI) to ASEAN by Source Country and Industry (in million US$)*.[Online] Available at: https://data.aseanstats.org/fdi-by-sources-and-sectors (Accessed 20/01/2023).

Ministry of Planning and Investment. (2023). Report on foreign direct investment of 2022. [Online] Available at: https://www.mpi.gov.vn/Pages/tinbai.aspx?idTin=56359&idcm=208 (Accessed 24/01/2023).

EU-ASEAN Business Council. (2019). *EU-ASEAN cooperation - key trade and investment statistics*. [Online] Available at: https://ec.europa.eu/eurostat/statistics-explained/index.php?title=EU-ASEAN_cooperation_-_key_trade_and_investment_statistics&oldid=497250#Foreign_direct_investment (Accessed 20/01/2022).

Eurostat. (2022). *EU direct investment flows, breakdown by partner country and economic activity (BPM6)*. [Online] Available at: https://ec.europa.eu/eurostat/databrowser/view/BOP_FDI6_FLOW__custom_3593204/default/table?lang=en (Accessed 23/01/2023).

Koslowski, B. (2022). *Current Status of German Investments in Vietnam 2022/23*. [Online] Available at:https://www.ahk-knowledgehub-vn.com/post/current-status-of-german-investments-in-vietnam-2022-23 (Accessed 24/01/2023).