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RECOGNIZING THE ROLE OF FDI AND THE REQUIREMENT OF INSTITUTIONAL REFORM IN VIETNAM

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Tóm tắt

Tưởng rằng gia nhập WTO sẽ có thể chắp thêm cánh cho kinh tế Việt Nam bay cao hơn nhưng thực tế lại không như mọi người kỳ vọng. Từ năm 2007 đến nay kinh tế Việt Nam liên tục đối mặt với tình trạng bất ổn vĩ mô, nhiều yếu kém của nền sản xuất nội địa bắt đầu bộc lộ. Trong khi các cỗ máy của tăng trưởng kinh tế trong nước như SOEs và doanh nghiệp nội địa gần như ngưng trệ thì doanh nghiệp FDI vẫn duy trì sức tăng trưởng của mình và tiếp tục có những đóng góp quan trọng cho kinh tế Việt Nam. Nghiên cứu của FETP (2013) chỉ ra những nút thắt thể chế đã khiến cho khu vực FDI không có động cơ tham gia vào các mắt xích của nền sản xuất nội địa nhưng cũng chính nhờ đó mà khu vực FDI gần như miễn nhiễm khỏi các trục trặc của nền kinh tế trong nước. Thừa nhận các yếu kém về mặt thể chế đang gây trở ngại cho phát triển kinh tế, Chính phủ Việt Nam đang thực hiện nhiều biện pháp nhằm cải cách thể chế nhưng đồng thời cũng nhìn nhận lại vai trò của FDI trong giai đoạn phát triển sắp tới của Việt Nam. Bài viết này sẽ trình bày khái lược về tình hình thu hút FDI ở Việt Nam kể từ khi Việt Nam thực hiện chiến lược đổi mới kinh tế năm 1986 theo mô hình kinh tế mở và hội nhập. Bài viết cũng phân tích những đóng góp của FDI đối với kinh tế Việt Nam, đồng thời chỉ ra những bất cập và hạn chế trong chiến lược hơn 25 năm thu hút FDI của Việt Nam. Cuối cùng, bài viết cũng sẽ phân tích những tranh luận gần đây trong giới học giả cũng như các nhà hoạch định chính sách Việt Nam về vai trò của FDI trong bối cảnh Việt Nam đang thực hiện chiến lực tái cơ cấu kinh tế gắn với mô hình tăng trưởng mới, đặc biệt là giai đoạn chuẩn bị tham gia TPP.

Abstract

It was expected that upon the inception of the World Trade Organization (WTO) that Vietnam's economy would sprout wings and soar to unexpected heights, but in all reality it was a disappointment. Since 2007, Vietnam's economy has faced several challenges that rumbled the macro stability and revealed the weaknesses of the real domestic sector. While local growth engines like State Owned Enterprises (SOE) and domestic firms were stagnant, the Foreign Direct Investment (FDI) sector maintained its growth momentum and continued to make important contributions to Vietnam's economy. According to a Fullbright Economics Teaching Program (FETP) study in 2013, there are institutional bottlenecks that discouraged the FDI sector to participate in the local production chain and unexpectedly immunized them from problems of the domestic economy. With respect to institutional weaknesses, as barriers to economic growth, the Vietnamese Government has implemented measures to reform these institutions and reviewed the role of FDI in Vietnam's next phase of development. In this report, I will briefly describe the FDI policy of Vietnam since Doi Moi (or Innovation) in 1986 toward an open and integrated economy. Further, I will analyze FDI contributions to the economy and show the problems and limitations of the last 25-years of FDI policy implementation. Lastly, this report will explore recent debates among academia and policy makers in Vietnam about the role of FDI as Vietnam attempts to restructure the economy and introduce a new growth model while finalizing Trans-Pacific Partnership (TPP) negotiations in the near future.

Keywords: FDI, Vietnam economy, capital inflows, institutional reform, FDI from Taiwan

1. Introduction

Vietnam's economic story begins in 1986 when Vietnam began implementing innovative policies and economic integration. In its earliest stages, the foreign investment sector was identified as one of the most important economic sectors in Vietnam's economy and contributed to the success of strategic industrialization and modernization undertaken by the Vietnamese Government. These innovative ideas, policies, and incentiveswere applied by the government at both the central and local levels to attract foreign investment. Nearly thirty years later, Vietnam has attracted more FDI than many other countries in the region in terms of Gross Domestic Product (GDP) percentage -- far exceeding Thailand, Indonesia, India, and even China. The cumulative foreign capital to GDP in Vietnam is much higher than those in other countries in the region, including China. Some studies show that FDI has made important contributions to Vietnam's economy in many aspects, such as complementary domestic savings, growth, economic structural change, improvement in the investment climate, strengthening of state governance, promotion of industrial policy, enhancement of national competitiveness, contributions to exports and revenues, job creation and improvement of salaries, etc. In addition to this success, further studies point out the inadequacies and limitations of FDI in Vietnam. These inadequacies and limitations include the fact that the majority of foreign enterprises employs only unskilled labor, engage in national resource extraction, uses outdated technology, contributes to environmental pollution, primarily uses imported resources, produces a low added value, provides poor spillover effects on domestic production, succumbs to restrictions on the Transfer of Technology (TOT), and so on.

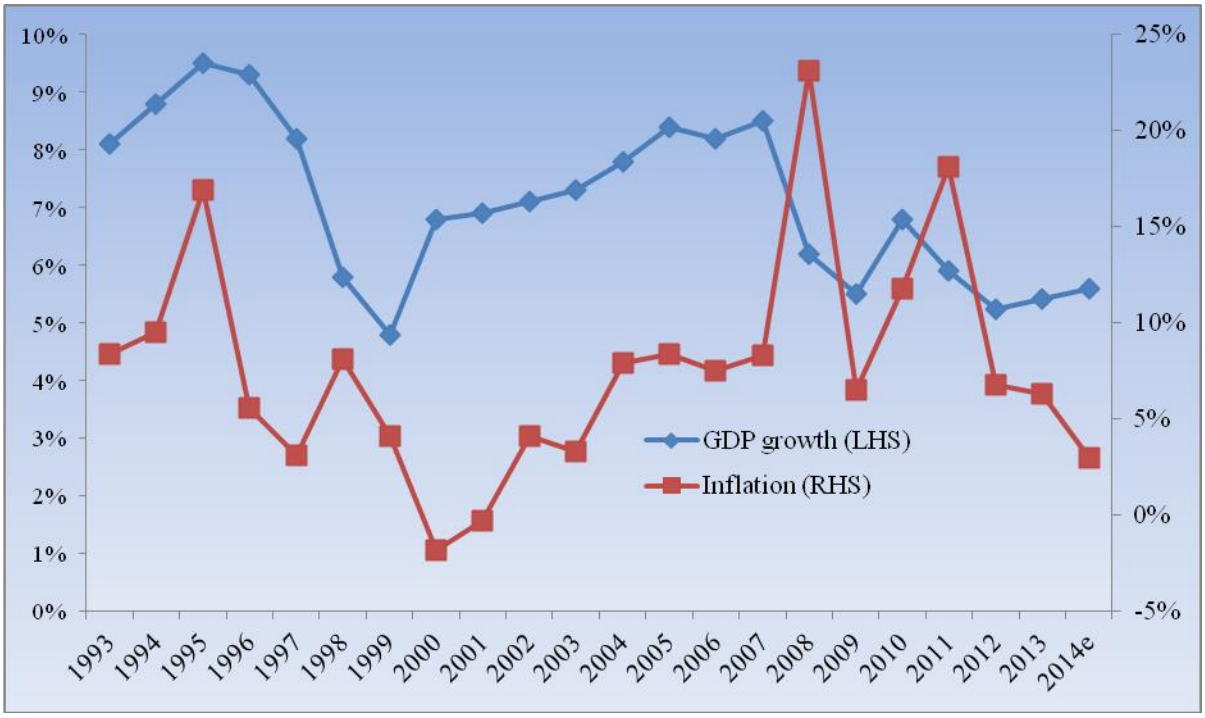
Especially in recent years, while Vietnam's economy has begun to fall into attenuation of economic growth and macroeconomic instability, the inadequacies and weaknessess of the domestic economy also unfold. Among the weaknessess I have pointed out, the biggest weakness is the economic institution. Through many years of innovation, the foundation of economic institution in Vietnam has not changed much - especially in terms of thinking. State economy and state ownership are and continue to be key roles in which SOEs are chosen as the leader of the economy despite the poor growth performance of this sector. Many analysts argue that the institutional bottlenecks, which not only hamper Vietnam's economic growth, but also reduces the potential contribution of the FDI on the domestic economy are responsible. Although, the Vietnamese Government has recognized these problems and is implementing economic reform policies in which institutional reform is considered as a breakthrough. The success of institutional reform will not only help create a new impetus for economic growth, but also to encourage foreign investors consider domestic production of products, participate in global production value chains, and mount the domestic production chain into the global production system.

2. A glance at Vietnam's macro-economic context

Vietnam's economy has achieved growth of 9-percent or more, but that was the story of the mid-1990s. In the years prior to joining the WTO, Vietnam's economy showed signs of acceleration in which growth was very high - as much as 8 - 8.5-percent - until officially joining the WTO in 2007. However, Vietnam's economy in fact did not take off as people expected. After reaching a peak growth in 2007, the economy began to decline and continued to plunge since then. Economic growth in Vietnam is always associated with the tale of high inflation. Obviously, this is not a new story, because it has been talked about in economic textbooks - this is a big challenge for Vietnam with respect to policy management. From 2007 to the present, the Government of Vietnam has repeatedly switched between the priority objective of

growth and inflation control. This change in policy objectives will certainly affect the business environment of enterprises in Vietnam - domestic investors as well as foreign investors.

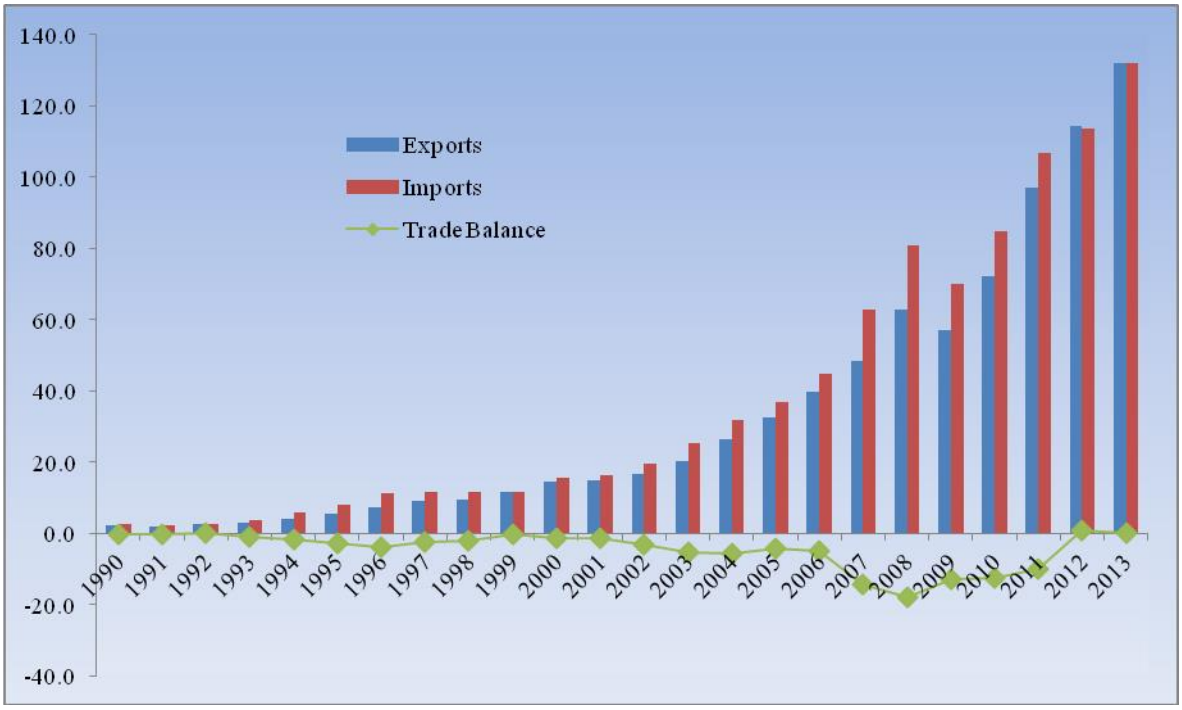
Figure 1: GDP growth and inflation in Vietnam



Source: GSO of Vietnam

In addition to inflation, the macroeconomic instability in Vietnam is also manifested in the severe trade deficit and enormous pressure on the devaluation of currency. The trade deficit has connotations that domestic savings are not enough to finance investment, but it also means that the competitiveness of Vietnam's economy is poor. As will be discussed later, foreign investment has partially improved Vietnam's export capacity, but it still does not fully compensate for the weakness of the domestic economy. The trade deficit has been financed mainly from foreign capital inflow. Unfortunately, the huge capital inflow has directly caused turmoil in Vietnam's financial markets. The Government of Vietnam has not had much experience in managing the flow of international capital while the openness of Vietnam's capital account increased significantly after joining the WTO. More than 9-billion US dollars poured into Vietnam's economy in the first half of 2007, this posed a huge challenge for monetary policy while Vietnam pursued a fixed exchange rate. Economists call this situation as a trilemma or an impossible trinity. Meanwhile the sterilization policy of the State Bank of Vietnam (SBV) was not effective when it could not sterilize the money supply and thus, inadvertently pushed the inflation rate to a very high level in 2007.

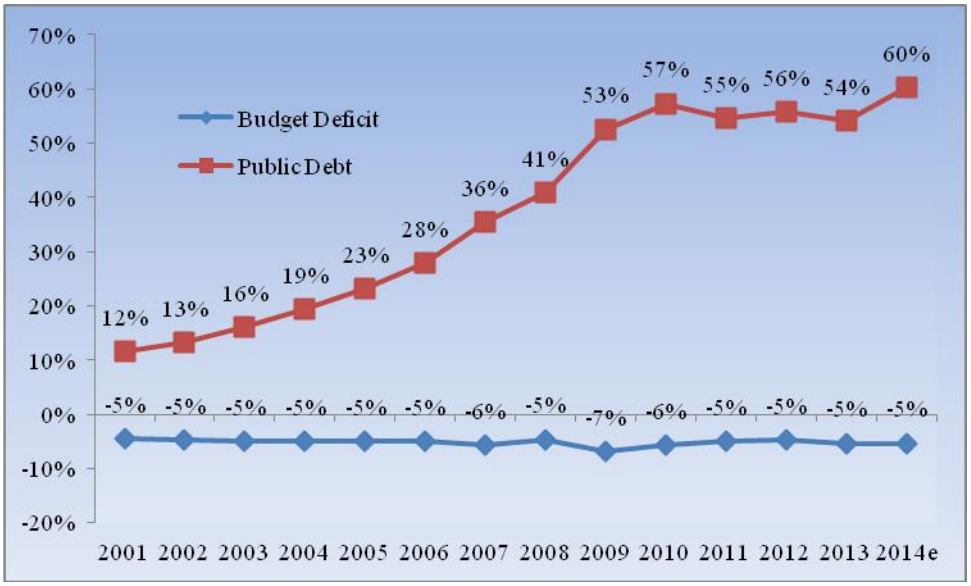
Figure 2: Trade Balance of Vietnam



Source: GSO of Vietnam

In addition to the trade deficit, the problems of the public sector such as budget deficits and the increase in public debt also exhibited a direct push on Vietnam's economy and yielded difficulties and uncertainties. The budget deficit of the Vietnamese Government has always been maintained at a very high level of 4 – 5-percent per year and this endured for a very long time. This has lifted the public debt which is currently equivalent to 60-percent of the GDP. The cause of the high budget deficit in Vietnam is partly due to budgetary discipline which is very loose. The mechanism of a soft budget constraint also raises a moral hazard in the public agencies that are funded by the national budget (Do Thien Anh Tuan 2014a). Moreover, the increase in Vietnam's public debt is also due to the Government's loans to finance public investment projects, but the efficiency is very low. SOEs also borrow money from banks, especially from the state-owned banks, to invest in a variety of projects and these loans are usually guaranteed by the Vietnamese Government. Meanwhile most SOEs have exhibited poor financial performance. After all, almost all of the international government bonds were transferred to the state business corporations, but the inefficient performance of these corporations has put a burden of debt on the Government's budget. A typical example is the bond debt worth US $750-million that the Government borrowed on the international bond market in 2005 and then lent it to Vinashin – a shipbuilding corporation of Vietnam – eventually this corporation was unable to repay the debt which led to a decline in Vietnam's credibility on the international capital markets.

Figure 3: Budget deficit and public debt in Vietnam (% of GDP)

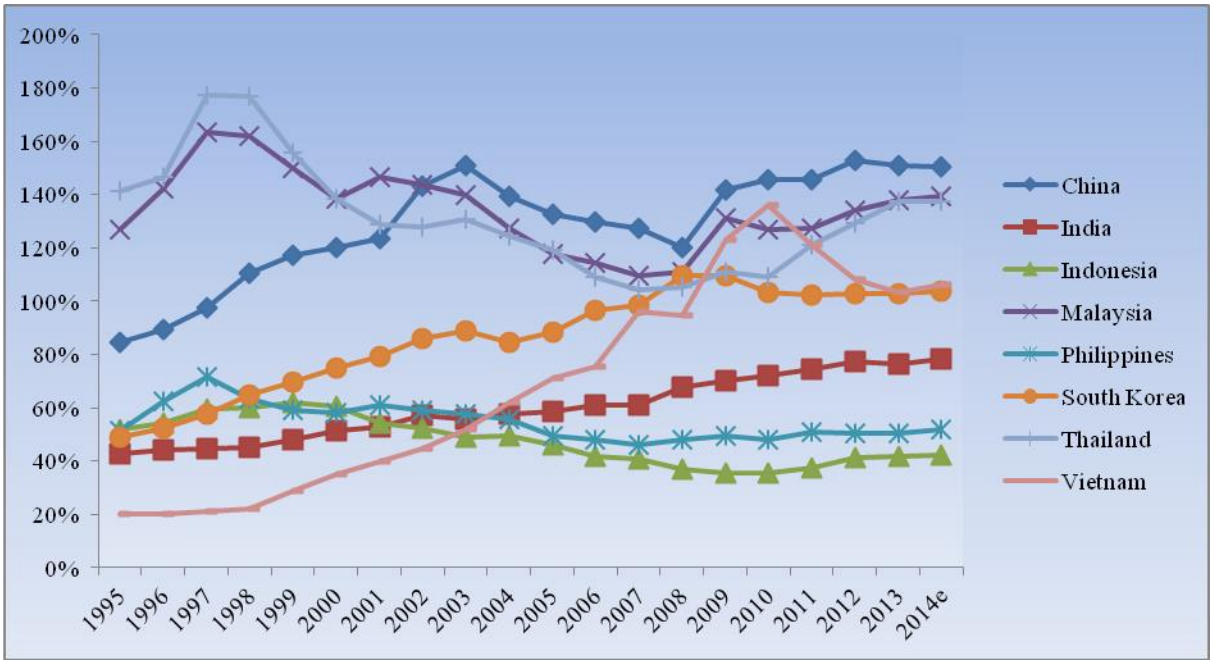


Source: MOF

Along with the weakness of the public sector, the Vietnam financial system also began staggering with difficulties - in particular the banking system. After a period of explosive growth in credit – as much as 30-percent to 50-percent in some years - credit growth has started to decline even though the rate of domestic credit to GDP in Vietnam has reached over 100-percent of GDP and has surpassed many countries in the region. Severe bad debts have pushed many banks in Vietnam to fall into serious financial difficulties. Meanwhile, the economic downturn also hindered the resolution of Non-performing Loans (NPLs) and the ability to restore stability of the balance sheets of banks (Do Thien Anh Tuan 2014a). The freezing of the real estate market and stock market also created its own difficulties, which in turn had an impact on the banking sector. A large amount of credit previously went into the real estate sector, but the freezing of the real estate market also placed a burden of liquidation on banks. Nevertheless, the situation of complex cross-ownership in Vietnam's banking system has caused the ineffectiveness of regulations on banking supervision of the SBV (FETP 2014).

The above analysis partially explains that, perhaps never, since the crisis of the mid-1980s, Vietnam's economy has fallen again into serious and prolonged instability as it has over the most recent past. Weakenesses of the old-style growth model, which is based on incremental invested capital, has not helped Vietnam in achieving higher growth. The Solow growth model seems to accurately predict the case of Vietnam - of course, this is just a hypothesis. So far, the Vietnamese Government has recognized the problems and has also developed and implemented projects to repair the economy, but the process is still very low compared to the requirements and expectations of many people for having various obstacles. It seems that the obstacles from the inside are significant enough that reform is almost at a standstill. The Government of Vietnam is currently negotiating to join the Agreement on the TPP and many people expect this Agreement will be a boost for Vietnam to promote reform.

Figure 4: Domestic Credit to GDP



Source: EIU

However, the question is how the TPP Agreement impact to Vietnam's economy is now still a debate among Vietnamese scholars and policy makers. Lessons learned from the WTO inclusion are certainly very valuable to businesses as well as the economic management agencies in Vietnam. As indicated, Vietnam's economy not only did not take off after joining the WTO, but it also faced many complex challenges. Joining the TPP may create similar or larger challenges. The big question here is whether a dose of the TPP is strong enough for the Vietnamese Government to discover the challenges and consider those as a driving force for economic reform at this time.

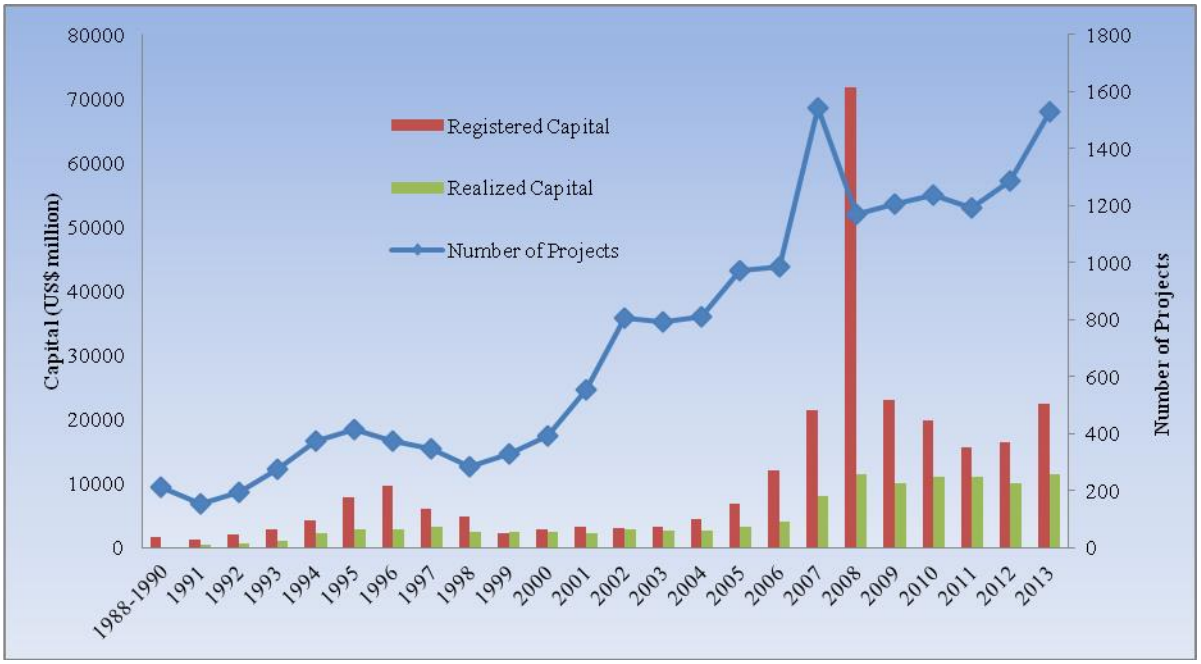
3. The process of opening up and attracting FDI in Vietnam

3.1. The period after Renovation of 1986 to the pre-Asian crisis in 1997

Vietnam has experienced almost 30 years of economic renovation and it has also been approximately that many years since the Government of Vietnam issued the first version of the Foreign Investment Law (FIL), which marked the establishment and integration of Vietnam into the world economy. During that time, policies to attract foreign investment into Vietnam have undergone positive changes which resulted in a wave of FDI flow into Vietnam in the context of the national and international economy. Figure 5 shows the process of attracting FDI into Vietnam for the period of 1988-2013. Only two years after the FIL was enacted, there were more than 200 foreign investment projects registered with a capital of over US $1.6-billion. This figure is not large in terms of absolute value, but when compared to the size of the economy in 1990 the ratio is equivalent to 25-percent which is quite impressive. Obviously, this was a success beyond expectations because in that context Vietnam's economy was facing many difficulties, inside was the macroeconomic instability and high inflation and outside was the collapse of COMECON along with the collapse of the socialist model in the Soviet Union and the Eastern European countries. Also during this period, there were economic sanctions imposed by the U.S. Government on Vietnam since reunification in 1975. During the period from 1992 to 1997, Vietnam's economy grew consistently very high, averaging nearly 8.8-percent each year. Even in the two years of 1995 and 1996, the growth rate

peaked at 9.54-percent and 9.34-percent, respectively. This result is partly due to policies unleashed in the private sector after a long time of constraint, but another part is the role of the foreign investment sector – which is like a catalyst for the reform of the business environment and the dynamics of competition for domestic businesses, as well as for the SOEs. The year 1995 was also a time when the United States and Vietnam declared normalization of diplomatic relations. This milestone not only marked a new phase in the history of relations between Vietnam and the U.S., but more importantly, it opened a new stage in the process of economic integration in Vietnam, to facilitate and attract more foreign investors throughout the world into Vietnam. FDI continued to flow into Vietnam in the following years and peaked in 1996 with a total registered capital of over US $9.6-billion before the start of a slowdown since 1997 when East Asian economies fell into crisis.

Figure 5: FDI flows into Vietnam period 1988 - 2013



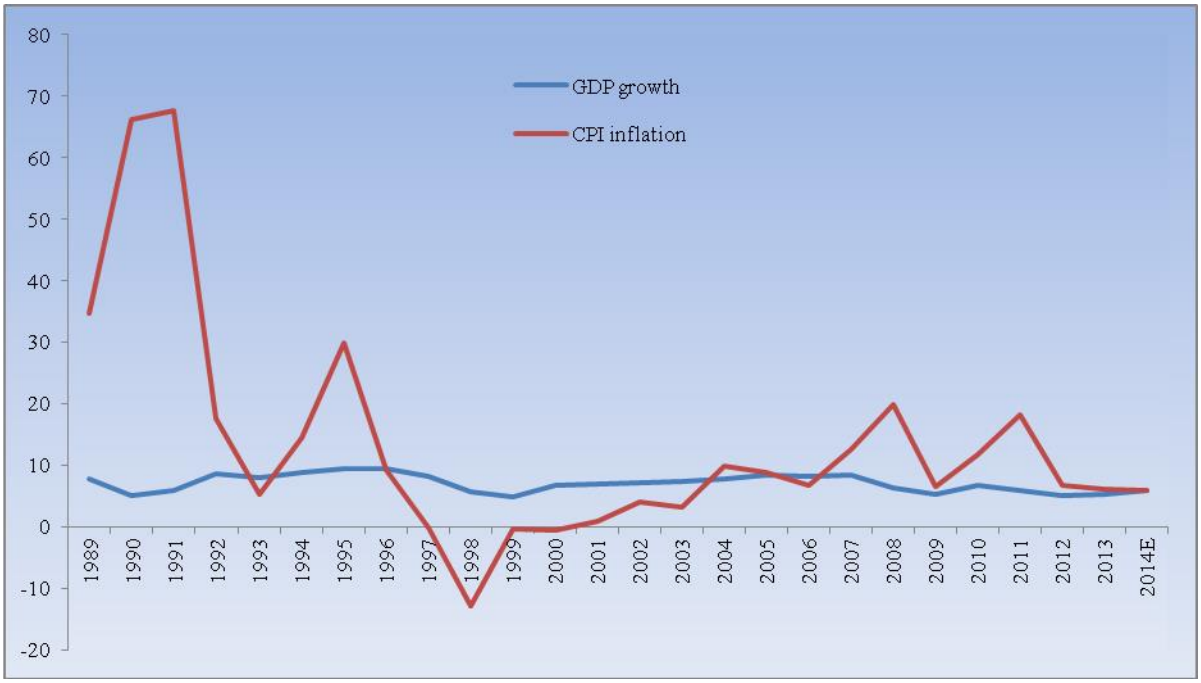
Source: Vietnam General Statistics Office

3.2. The period after the East Asian crisis until before joining the WTO

Until the mid-1990s, Vietnam's economy had not yet fully integrated into the world economy, but the impact of the Asian financial crisis in 1997 on the economy of Vietnam was very clear, if we look at the decline of inflows of FDI. This period of decline lasted until 1999 when the amount of registered capital was just US $2.3-billion - equivalent to that of 1992. Not only the registered capital, but also the number of foreign projects decreased as well. The number of foreign projects, after peaking in 1995 with 415 projects, fell back to only 285 projects in 1998. In addition to the impact of the Asian crisis, the amendments to the Law on Foreign Investment in 1996 could also be a cause of the decline of foreign investment inflows into Vietnam during this period. This is because the amended FIL has reduced the incentives for foreign investors. Since 1999, the number of foreign investment projects began to increase rapidly, but the registered capital has almost not improved significantly. This situation maintained itself until 2006 when Vietnam was preparing to join the WTO. There was a notable point in attracting FDI in Vietnam during this period that the registered capital experienced greater volatility than the disbursement capital. This is true for both periods before and after the Asian crisis. There were even a number of years, while the

registered capital declined, in which the disbursement capital increased. This suggests that many foreign investors in Vietnam, in this period, were not affected much from the crisis or the continued disbursement of foreign capital and also showed that Vietnam was not affected much from this crisis. This has contributed to maintaining the trust and the growth rate for Vietnam's economy even during the economic crisis.

Figure 6: GDP growth and CPI inflation in Vietnam period 1988 - 2014



Source: Vietnam General Statistics Office

The recovery process of FDI in Vietnam took place simultaneously and at the same pace with the recovery of Vietnam's economy during the period 1999-2006. Figure 6 shows that Vietnam's economy declined sharply in 1999, but has recovered at a reasonable pace before joining to the WTO at the end of 2006. Both the number of projects and the registered capital accelerated in 2006, signaling a new boom of FDI as had occurred in the later years of innovation. Despite this, registered capital and the number of projects simultaneously tended to increase, but the disbursements did not increase significantly. Although this means that many foreign investors have begun to expect a brighter future for Vietnam's economy, an all-clear signal to realize investment opportunities in Vietnam has not yet transpired. Vietnam becoming the 150th member of the WTO in late 2006 officially transmitted a positive signal to the expectation of the international investment community.

3.3. The post-WTO period to the present

While it is difficult to describe all the excitement of the businesses and the investors when Vietnam officially joined the WTO, foreign investment capital started pouring into Vietnam - especially in the second half of 2006. Although the number of projects did not spike compared with the previous year, the registered capital continuously increased from US $6- billion in 2005 to more than US $12-billion in 2006, then US $21-billion in 2007, and peaked at US $71.7-billion in 2008, equivalent to 80-percent of the GDP of Vietnam in 2008. Although the actual disbursement of capital was lower than the registered capital, it

increased sharply compared with the previous period. The total value of FDI disbursed reached more than US $8-billion in 2007, rose to US $11.5-billion in 2008 and maintained at approximately US $10-billion to 11-billion per year to date even when the registered capital began, and continued to decrease in and since 2009.

The decline of registered FDI into Vietnam is partly due to the high growth of FDI inflows in the initial years of the post-WTO era. Since 2009, even the registered capital has had a tendency to decline, but it still remains at a higher level than the period before WTO accession. Otherwise, the drop of FDI registered during this period is part of the reason that many foreign investors are affected by the economic crisis, which is considered the worst since the Great Depression 1929-1933. This reason may be true in part because the rate of disbursement to registered capital in this period is quite low, only 35-percent, just half of the rate during the period before WTO accession. However, the actual funds disbursed in this period are very large compared to the scale and the absorption capacity of Vietnam's economy in a short amount of time. This does not take into account the huge amount of Foreign Indirect Investment (FII) that poured into Vietnam during this period, which is estimated by the SBV to be as much as US $6.25-billion. In addition to the investment capital flows, other flows such as remittances and official aids also increased sharply during this period. When capital flows into a country it will pose many challenges for policymakers to stabilize and manage the macro economy. In Vietnam, the exchange rate mechanism is maintained almost constant by the SBV. In the context of free capital flows, it will make monetary policy ineffective. This is the challenge of the impossible trinity situation that Vietnam's policymakers have actually faced during this period. As shown in Figure 6, the high inflation rate flared up again when the SBV was unable to sterilize a huge amount of the money supply that this agency had pumped out to buy a large amount of foreign reserves in order to prevent the appreciation of the currency.

Fortunately, many foreign investment projects continued to rise steadily while Vietnam's economy fell into turmoil and the many weaknesses of the domestic economy began to emerge. This suggests that foreign investors do not pay much attention to the weaknesses of Vietnam's domestic economy. This assertion may incite controversy because the problems of the economy will inevitably affect the investment climate and the competitiveness of businesses (particularly foreign enterprises) in general. However, as many studies have shown,[3] this still may be true in the context of Vietnam as the institutional weaknesses have led to a lack of incentives for many foreign businesses to mount their operations into the domestic production system. In other words, the links in business activities of foreign and domestic firms are very loose and the limited application of Vietnam's institutional provisions on foreign firms "granted" immunity from the weaknesses of domestic institutions. This fact poses new challenges for the Vietnamese Government to recognize the role of FDI in Vietnam, as well as the requirements for institutional reforms aiming not only at attracting FDI to be more compatible with the goal of economic development, but also create new momentum for sustainable economic growth in the future.

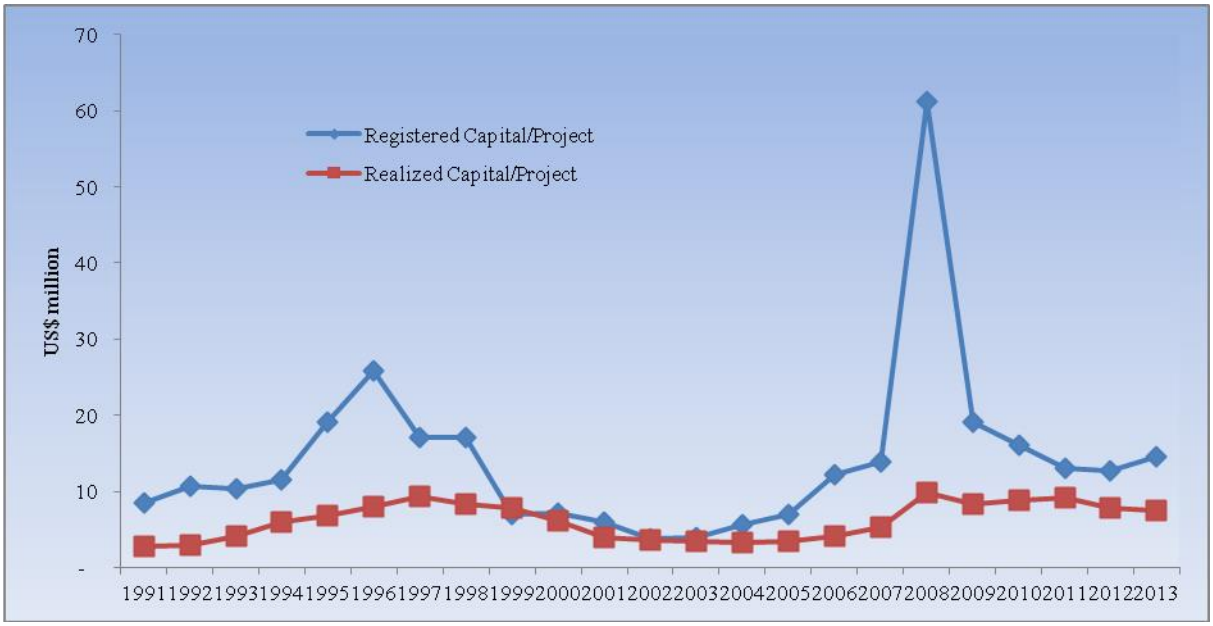
[3] See FETP/VELP 2013.

4. Some characteristics of FDI in Vietnam

4.1. Scale of projects

By the end of 2013, Vietnam has attracted nearly 16,000 foreign investment projects with a total registered capital of US $234-billion. But on average, the size of an FDI project in Vietnam is relatively small. Most foreign investors to Vietnam are mainly small and medium-scale enterprises coming from countries in the region. Over a span of 23 years (1991-2013), the average registered capital of one project is approximately US $14-million. If it is calculated separately for the actual disbursement, the size of one project is much smaller - approximately US $6-million. The average scale of projects varies over time, especially before and after an economic crisis.

Figure 7: Scale of projects



Source: Calculated from database of Vietnam General Statistics Office

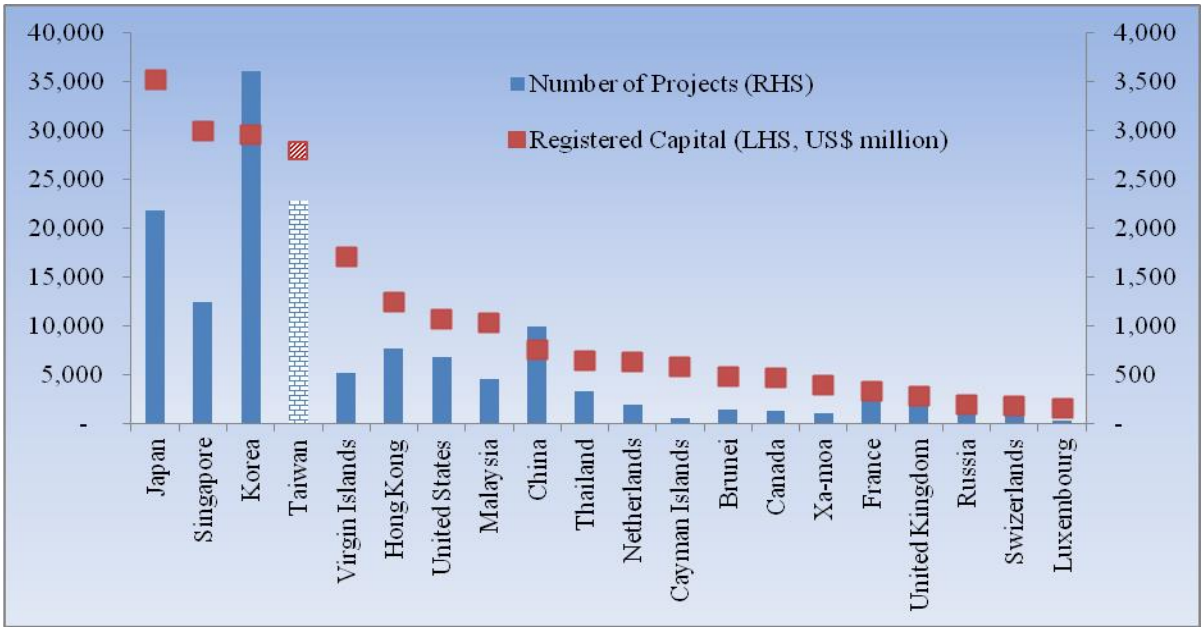
Prior to the East Asian Crisis, 1991-1997, the average capital scale of one foreign project had increased from US $3-million to US $9-million. The scale of projects began to decline during the recession - down to an average of approximately US $3.5-million a project - and continued plummet until 2005. After joining the WTO, project size began to increase and peaked in 2008 at US $10-million a project if calculated based on disbursement or US $61-million based on registered capital. The scale of foreign projects has had a tendancy to backslide slightly from 2009, reaching an average of about US $7.5-million a project.

4.2. Partners

Foreign investors in Vietnam come from many countries around the world with the most coming from the Asian countries of Japan, Korea, Taiwan, Singapore, Malaysia, China, etc. with a registered capital accounting for 70-percent of the total foreign direct investment capital. By the end of 2013, Japan was the largest foreign investor in Vietnam with an accumulative registered capital of over US $35-billion. Following Japan are Singapore (US $30-billion), Korea (US $29.6-billion), and Taiwan (US $28-billion). Although the total number of partners have invested in Vietnam is now greater than 100 countries and territories. However, there is a very high focus on a certain group of countries, particularly the countries

in the Asian region. Only ten leading countries investing in Vietnam have accounted for 80-percent of the total registered capital. This figure has virtually remained unchanged for more than two decades of attracting FDI in Vietnam. If calculated according to the number of projects, Korea, followed by Taiwan, Japan, and Singapore are the largest investors. These are also the top four countries that have invested the most in Vietnam. However, if calculated according to the average capital size of a project, these countries do not appear on the list. Instead, the British West Indies, Cayman Islands, Cyprus, and Luxembourg are the territories that have the largest project in terms of average capital scale. The average size of a project amongst all investors, coming from the U.S. or Euopean Union (EU) such as Germany, England, or France, is not too high if not lower than that of the investors from the Asian region.

Figure 8: Foreign Investment by Partners



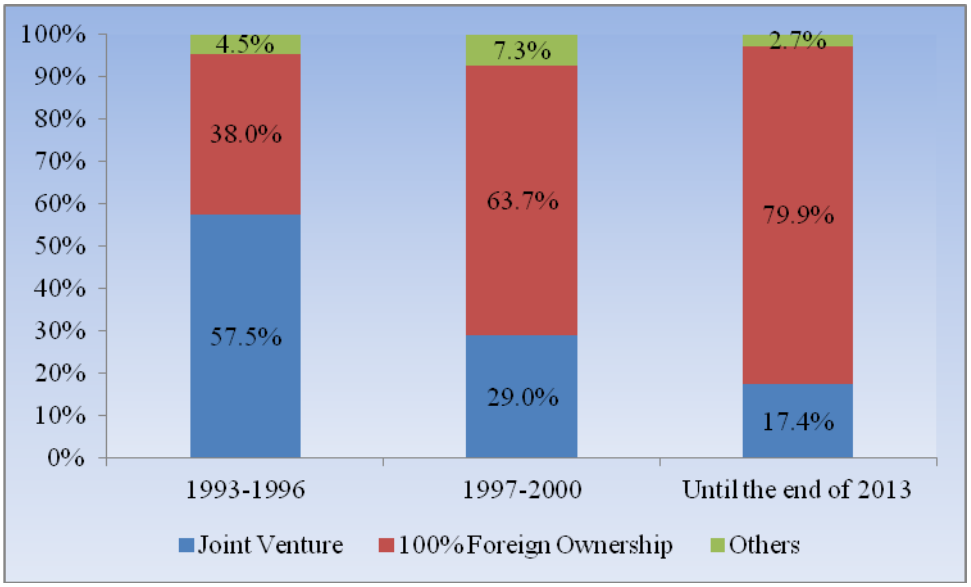
Source: Vietnam General Statistics Office

4.3. Form of ownership

There are many diffirent forms of ownership in the foreign invested enterprises in Vietnam, of which the most common are joint stock ventures and 100-percent foreign owned. other forms of ownership include business cooperation contracts and joint stock corporations. By the end of 2013, nearly 80-percent of all foreign projects organized were in the form of 100-percent foreign ownership, followed by joint stock ventures, accounting for 17.5-percent, and the remaining fractions are other forms of ownership. Foreign investment projects have changed significantly over time. Initially, due to myriad obstacles and various conditions, the FIL did not encourage investors to establish enterprises in the form of 100-percent foreign capital; instead the form of a joint stock venture between SOEs and foreign investors was very popular. Not until the mid-1990s, did the number of projects in the form of joint stock ventures account for 57.5-percent of total projects invested in Vietnam - only 38-percent of those projects were 100-percent owned by foreigners. Since 1997, after an amendment of the Law on Foreign Investment, limitations on ownership for foreign investors were gradually suspended. The form of ownership in the FDI projects also began to change dramatically. Up until the early 2000s, 100-percent foreign ownership had

accounted for nearly 64-percent of total FDI projects invested in Vietnam, while the number of joint stock venture projects had fallen to 29-percent. This propensity of shifting has continued until today.

Figure 9: Form of Ownership of FDI Projects



Source: Vietnam's Ministry of Planning and Investment

4.4. Field of Investment

FDI projects in Vietnam are spread across many fields and sectors ranging from agriculture to industry and services in which the number of registered projects in the field of manufacturing and processing industry has always accounted for the largest portion. The total number of projects in the field of manufacturing and processing industry accounted for nearly 55-percent of total projects and 54-percent of total registered capital by the end of 2013. The FDI capital primarily invested in the area of manufacturing and processing is essentially consistent with the direction of the industrialization policy in Vietnam. Although it is unlikely to generate a boom in Vietnamese Industry, it will at least contribute to the shifting of the economic structure of Vietnam towards industrialization. In the 1990s, FDI capital was primarily directed to the mining industry and import substituted sectors, however, many FDI projects are now strongly redirected to the manufacturing and processing industries and the export-oriented sectors. Considering that in some ways this shift is positive. FDEs have contributed significantly to the annual export turnover with the contribution ratio at approximately 60-percent to 65-percent of the total exports of the entire economy.

While the amount of capital registered in the industrial sector in general - manufacturing and processing sector in particular - tends to increase, the amount of FDI capital in the agricultural sector tends to decrease. Projects invested in agriculture, forestry and fisheries by the end of 2013 have accounted for only 3.1-percent of total foreign projects and 1.4-percent of the total foreign registered capital -- significantly lower than the corresponding rate of 17.3-percent and 8-percent in the mid-1990s and 8.8-percent and 5.6-percent in the mid-2000s. Foreign investment projects in the real estate area have increased dramatically since joining the WTO. There are currently over 400 FDI projects in the area of real estate business, accounting for approximately 2.6-percent of total projects, but the amount of registered

capital accounts for only 21-percent of the total cumulative registered capital by the end of 2013 - equivalent to more than US $49-billion.

Although FDI capital primarily flows into the manufacturing and processing sectors, the average capital size of one project is relatively small at approximately US $14.4-million. The average size of one project in the agricultural sector is much lower at only US $6.7-million. Meanwhile, the registered capital of one foreign real estate project is more than US $120-million. Similarly, mining projects have an average capital of US $40-million per project; the projects in other industries such as production and distribution of electricity, gas, etc. have an average capital of more than US $100-million each project.

4.5. Investment location

All localities in Vietnam have attracted FDI capital, but capital distribution is uneven. FDI is mainly concentrated in some regions with better conditions of infrastructure, skilled labor, and a good business environment. By the end of 2013, Ho Chi Minh City, Ba Ria – Vung Tau, Ha Noi, Dong Nai, and Binh Duong are the top five provinces attracting the most FDI capital in Vietnam. These five localities have attracted more than 50-percent of the total FDI capital in the country. In recent years, the distribution of FDI was more balanced. Many other provinces have strongly emerged, increased their investments in infrastructure and implemented the best preferential policies to attract big investors throughout the world. It is the dynamic of these localities that has made them appealing to big investors in attracting FDI. It is no longer the exclusive playground of traditional localities. Although not entirely true for all localities, especially localities in the Northwest, the Central Highlands, and the Mekong Delta, FDI capital has a more harmonious distribution among localities. Many localities have been racing to build industrial parks and compete with each other in various ways to fill up those parks. Many localities, however, due to poor planning and planning not based on any particular competitive advantages; rely heavily on the preferences of land, taxes, and infrastructure. Consequently, many industrial parks have been established and then abandoned. Unhealthy competition policies among localities have accidentally pushed all localities to fail altogether into situations of disadvantage and cause damage to the overall benefit of the economy (Vu Thanh Tu Anh 2006).

4.6. Attracting large international corporations

As previously discussed, the majority of foreign investors to Vietnam are small and medium enterprises coming from surrounding Asian countries. Apparently, small enterprises have their own advantages, but generally small scale companies might face many disadvantages in the competition, especially when they want to reach out and join the world economy. Vietnam is now trying to attach its domestic production chain to the value chain of the global production system. To achieve this goal, the role of transnational corporations is very important. These corporations are expected to not only help domestic enterprises access the global market, but also help to create momentum for economic reform and stronger competition, even in the domestic market.

For a long time after opening the economy and attracting FDI, Vietnam continues to lack world-class investors. In the most recent decades, the active participation in trade and investment agreements with many countries has created many opportunities for Vietnam in attracting the world's largest corporations. So far, Vietnam has attracted over 100 out of more than 500 of the world's leading transnational corporations. Many of the leading corporations in the world such as BP, Total, Intel, Unilever, Coca-Cola, Pepsi, Samsung, Nokia, Toyota, and Canon have come to Vietnam which has

provided opportunities for Vietnam to upgrade the value chain of the domestic production system. Can Vietnam be successful or not? The answer depends on many factors of which the most important thing is the capacity of domestic firms. Whether these firms can be upgraded to keep pace with the demands of global standards or not? Additionally, institutional reforms that encourage pursuing Vietnam is also considered as a prerequisites. Because these reforms will not only help Vietnam attract more top foreign investors, but more importantly, create a new growth engine for the domestic private sector. The Vietnamese industrialization policy cannot be called successful if the game has only the world's leading corporations, but lacks domestic industrialists.

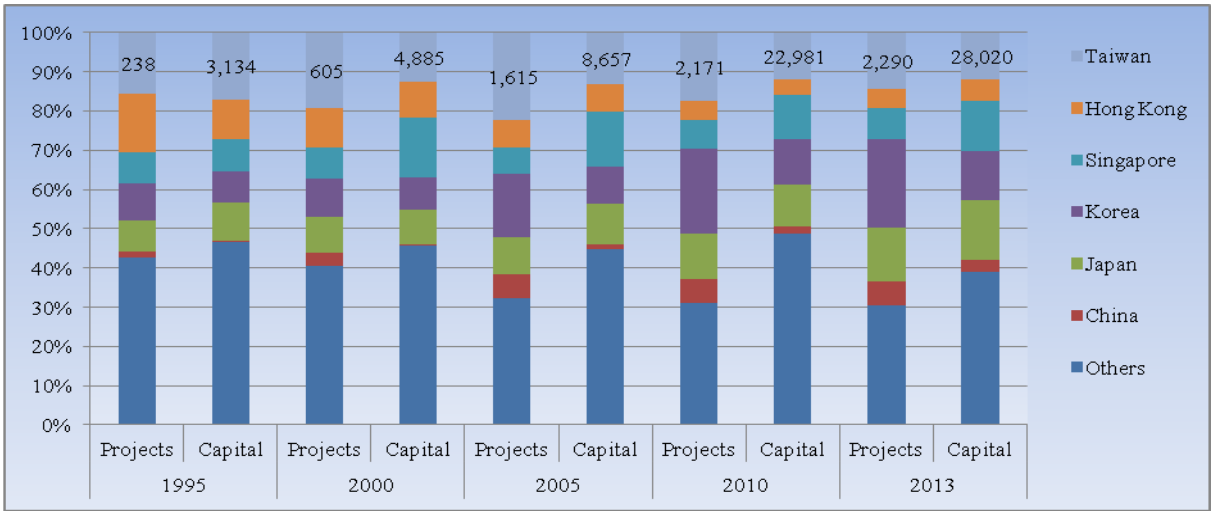
4.7. Taiwan's direct investment in Vietnam

Investment of Taiwan enterprises in Vietnam

Taiwan is one of the most important ecnomic partners of Vietnam on various aspects from trade to investment. Since opening up and attacting FDI to date, Taiwan is always among the top leading countries and territories that have many projects invested in Vietnam. By the mid-1990s, Taiwan had a total of 240 projects with a total registered capital of over US $3-billion, accounting for 17-percent of total FDI capital in Vietnam - the leader of all the countries/territories that had investment projects in Vietnam. By the mid-2000s, the total number of projects that Taiwan had invested in Vietnam exceeded 1,600 projects and accounted for 22-percent of total foreign projects with a total registered capital of US $8.6-billion which accounted for 13-percent. Until the end of 2013, Taiwan continued to maintain its position as one of the four largest foreign investors in Vietnam, just behind Japan, Singapore, and South Korea in terms of registered capital. Up to now, the total number of Taiwanese enterprise projects invested in Vietnam has risen to nearly 2,300 projects with a total registered capital exceeding US $28-billion, ranking second only to South Korea which has invested in 3,600 projects in Vietnam. Investments of Taiwanese enterprises is distributed throughout the most important economic sectors in Vietnam, including agriculture, manufacturing and processing industries, mining, transportation, construction, hotels, tourism, etc. As of the end of October 2014, Taiwanese enterprises have invested in 60 new projects and increased capital in 44 operating projects with a total new capital investment of US $723.4-million and now ranks 5th out of 56 countries and territories that have projects in Vietnam. Investments of Taiwanese enterprises continue to focus on the manufacturing and processing sector. There are 40 new projects and 40 new capital projects with a new total of registered capital reaching US $670.5-million. Following this are accommodations, food, and buildings. As for the agricultural sector, Taiwan is currently in the leading position and more than 30 countries and territories have invested in Vietnam's agricultural sector.

Taiwan's investment projects are now established in over 50 of Vietnam's provinces, but are mainly concentrated in the Southern provinces such as Ho Chi Minh City, Dong Nai, Binh Duong, and Long An. In the first ten months of 2014, 24 provinces attracted investment from Taiwan, in which Ha Nam and Dong Nai are the two provinces in the lead. Taiwanese firms employ about 100.000 direct workers and tens of thousands of indirect workers.

Figure 10: FDI from Taiwan compared with other countries/regions (US$ Million)



Source: Vietnam's Ministry of Planning and Investment

Vietnam as a preferred destination for Taiwanese enterprises

According to the survey results of the Ministry of Economic Affairs of Taiwan, Vietnam remains an important investment destination for Taiwanese enterprises in the next three years. In comparison with China, Vietnam ranks behind by only three coastal economic zones of China, including Jiangsu, Guangdong, and Shanghai. The motivation for choosing Vietnam as the investment destination of Taiwanese enterprises focuses on the following four factors: (i) low labor costs; (ii) low land costs, tariff references and other incentives; (iii) exploitation of the potential of markets; and (iv) meeting the requirements of shift in the supply chain.

However, according to the survey on the Taiwanese enterprises in 2007 and 2011, the important and priority position in the aforementioned factors have changed noticeably. Accordingly, while the low cost of labor is still the leading factor in the decisions of Taiwanese firms, the cost of land and other incentives has become a secondary factor.

In addition, the development potential of Vietnam's domestic market is also an important factor for Taiwanese businesses. In 2007, this factor was ranked at 4, but in 2011, the position improved to a ranking 2. This suggests that the shift to accessing Vietnam's market is becoming clearer (IPCS 2012). The ability to access natural resources is also an important engine in the investment decisions of Taiwanese investors. After a disquieting event in the East Sea, Taiwanese businesses remain confident of Vietnam's investment environment. Investment flows from Taiwan in the near future will continue to pour into Vietnam as a stable and reliable destination. The fields in which Taiwanese investors are now interested in include insurance, medical equipment, electrical equipment, automotive parts, food, cosmetics, and more.

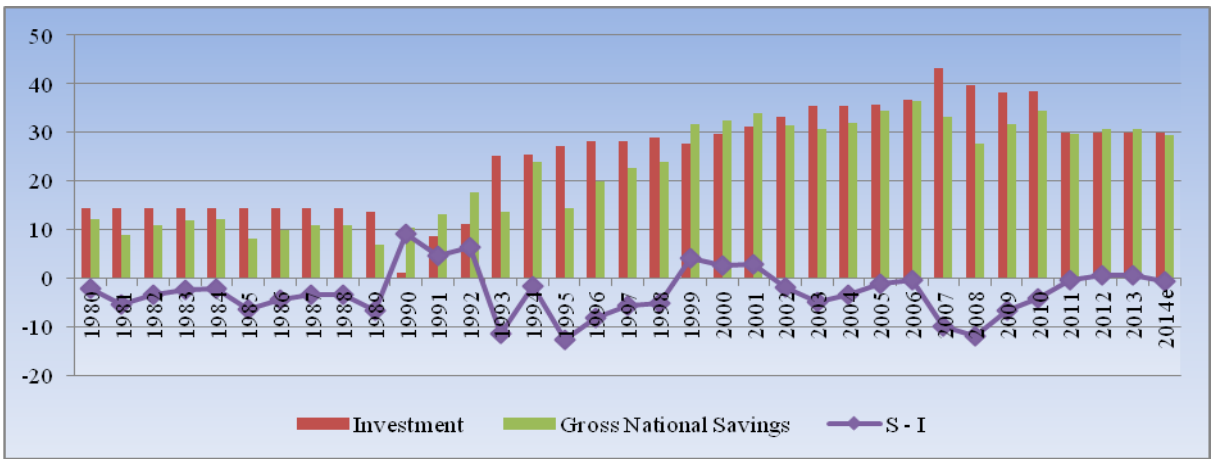
5. The role of FDI in the Vietnam's economy

5.1. Additional investment capital for the economy

As a developing country, Vietnam needs huge investment for economic growth. Meanwhile, the scale of domestic savings is often not sufficient even if the rate of savings in Vietnam is relatively high. Therefore,

the attraction of foreign investment is also a way to supplement national savings and increase investment capital for economic development in Vietnam. With that in mind, from very early on, the Vietnamese Governments reform policies have focused on attracting international capital, with a special emphasis on the role of FDI.

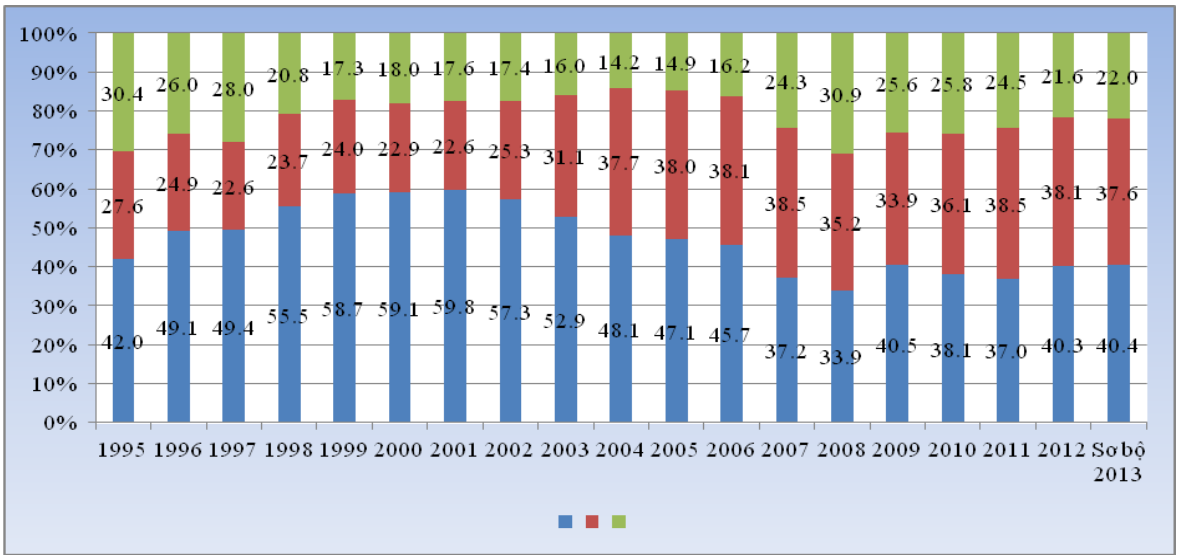
Figure 11: Gross National Savings and Investment of Vietnam (% of GDP)



Source: GSO of Vietnam

Figure 12 shows that the share of FDI capital in the total investment capital in the economy had reached approximately 30-percent in the period before the East Asian Crisis in 1997. After the crisis, along with private sector investment, the share of FDI capital began to decline similar to that period of time prior to WTO induction in 2006. After joining the WTO, the FDI share increased rapidly to peak like the period before the East Asian Crisis. The increase of FDI capital has coincided with the continuous growth of the private sector in the economy, while the role of the state sector has continuously declined since the beginning of the decade 2000. Currently the FDI sector is contributing more than one-fifth of the total investment capital of the economy as a whole.

Figure 12: Investment Capital by Economic Sectors



Source: GSO of Vietnam

5.2. Growth and the economic structure shift

Over the past decade, the FDI sector has always had the important contribution to GDP and GDP growth in Vietnam. Futhermore, the contribution of the FDI sector tended to increase, though the contribution proportion is still lower than that of the other two economic sectors. As Table 1 shows in the period 2001-2006, the FDI sector has contributed about 14.7-percent to the annual GDP of Vietnam, and increased to 17.6-percent in the period of 2007-2012. The contribution to the FDI sector to annual GDP growth was even greater and accounted for about 15.6-percent in the period of 2001-2006 and increased to 21.2-percent in the period of 2007-2012.

According to Dao Quang Thu (2013), FDI capital mainly focuses on the industrial and construction sectors with proportion of 58.4-percent, in which the technogical level of foreign enterprises is higher than the national average level. The growth rate of the industrial and construction sectors has reached an average of 18-percent per year, higher than the average growth rate of the entire industry. Similarly, in the agricultural sector, FDEs also contributed significantly to the trend of agricultural structure shift, diversification of products, improvement of the export value of agricultural goods, improvement of cultivation practices, absorption and application of advanced technologies in the field of agriculture, improvement of agricultural infrastructure, etc. Finally, foreign investors also create a new face in Vietnam's service sector. High-quality services such as hotels, restaurants, offices for lease, finance, banking, insurance, audit, legal services, shipping, logistics, supermarkets, etc. are increasingly attracting more foreign investors to participate in them, thus contributing to creating a competitive environment for businesses in the country while improving quality and service standards (Dao Quang Thu 2013).

Table 1: Overview of resource use and contributions of the three economic sectors

	State Economic Sector		**Non-State Economic Sector**		**Foreign Economic Sector**	
	2001-2006	2007-2012	2001-2006	2007-2012	2001-2006	2007-2012
Resource use						
Investment Capital	51.8%	37.4%	32.1%	36.8%	16.1%	25.7%
Capital per enterprise (US$ mill.)	12.9	53.4	0.26	0.91	6.77	10.8
Contributions to the economy						
GDP	38.2%	34.0%	47.1%	48.4%	14.7%	17.6%
GDP Growth	39.2%	27.6%	45.2%	51.2%	15.6%	21.2%
Revenues (exclude oil) – of total revenues	18.7%	17.9%	7.2%	10.7%	7.0%	11.1%
Jobs	11.8%	10.6%	86.3%	86.0%	1.9%	3.4%
Jobs Growth	8.4%	6.0%	77.8%	88.8%	13.8%	5.2%
Industrial Production Value	27.6%	18.2%	29.2%	37.5%	43.0%	44.2%
Industrial Production Value Growth	25.7%	11.7%	35.7%	40.4%	38.6%	47.9%

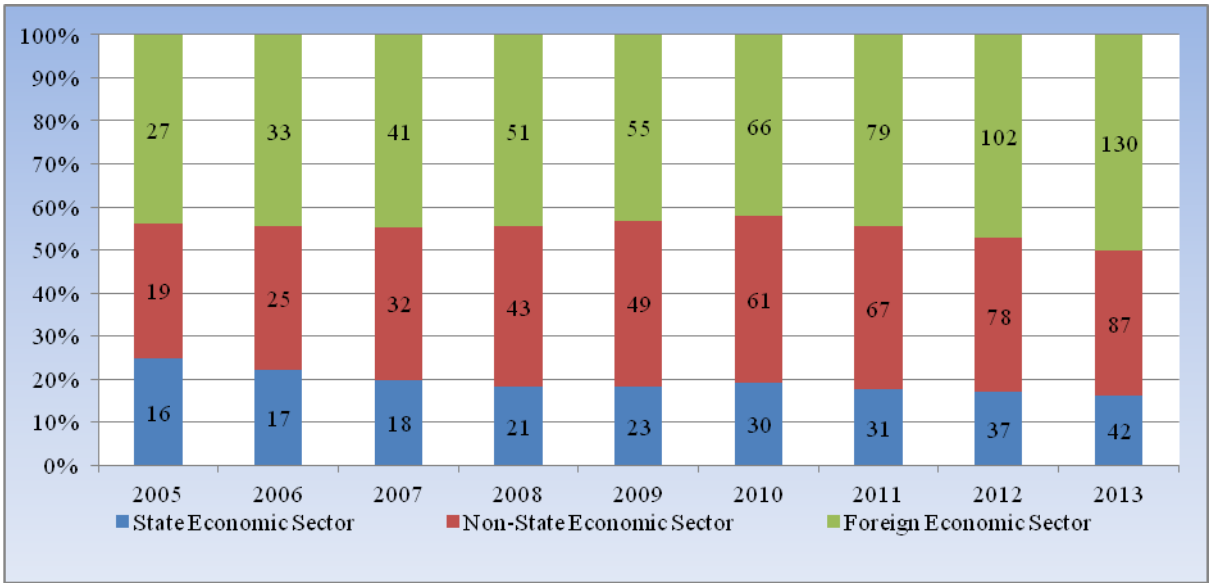
Source: FETP's calculation

5.3. Industrial policy

At an early age, after the adoption of the policy on innovation in 1986, the Vietnamese Government embarked on the implementation of industrial policy. To date, Vietnam's policy on industrialization has been just going a short journey, and the next journey is still very long, difficult, and challenging. The risks

of the industrialization policy of Vietnam are that it places its success or failure on the role of State-Owned Enterprises (SOEs). In fact, the role of SOEs as a driver of economic growth as well as industrialization strategy in Vietnam has been proven to be failure (FETP 2013). Meanwhile, the role of the private sector, so far, is still limited, although this sector is gradually revealing a more important role. In contrast, the FDI sector has contributed greatly to the initial success of the industrialization policy in Vietnam. As discussed above, FDI firms primarily invest in the industrial sector, thereby significantly helping to improve production capacity and efficiency of the industry in Vietnam.

Figure 13: Industrial Production Value by Sectors (US$ billion)



Source: GSO of Vietnam

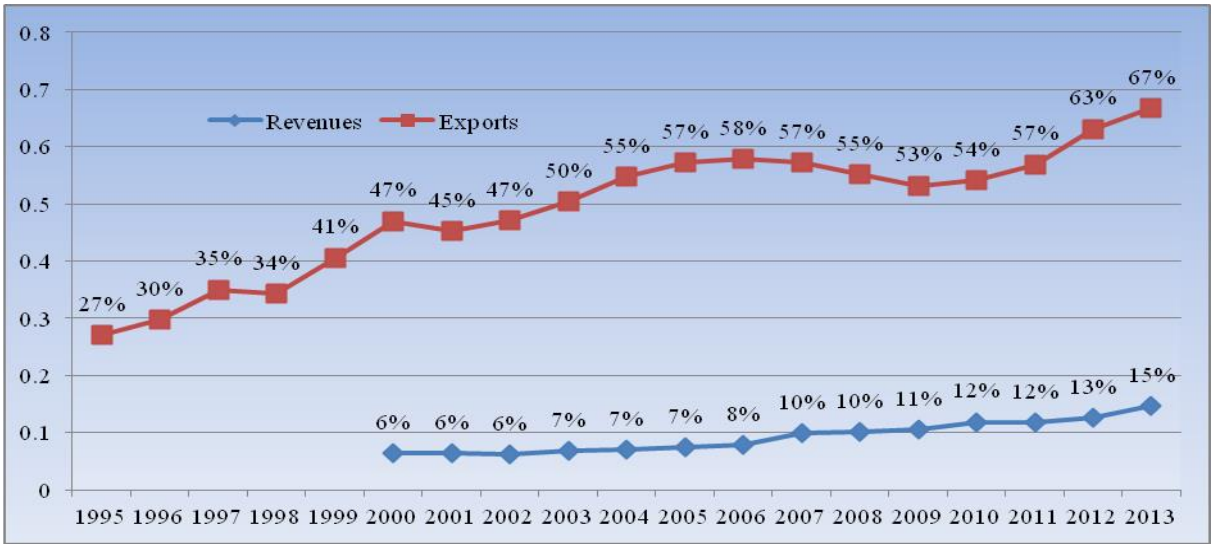
The data in Table 1 reveals that in the period 2007 – 2012, the FDI sector had contributed to more than 44.2-percent of the total value of industrial production, which appears to have increased significantly if it is compared with the 43-percent of the 2001-2006 period. Meanwhile, the state sector and the non-state sector had just contributed only 18.2-percent and 37.5-percent of the total value of industrial production during the period 2007-2012, respectively. Particularly in 2013, the industrial production value that the FDI sector generated is more than half of the total value of industrial production of the whole economy (see Figure **13**). The contribution to the growth of industrial production value of the FDI sector in the period 2007-2012 was higher than that of the previous period and reached 48-percent, while the state sector had accounted for 11.7-percent and the private sector accounted for 40.4-percent of the industrial production growth value. The remarkable thing is the percentage contribution from the FDI sector is very large, but the level of use of resources for this sector is the lowest compared with the other two sectors. Table 1 shows that the proportion of FDI capital accounted for only 25.7-percent of the total investment capital in the economy while the remaining two sectors, each accounted for approximately 37-percent of the total capital.

5.4. Tax revenues and exports

The FDI sector has contributed significantly to the annual national budget revenues in Vietnam. According to the Vietnam Ministry of Finance (MOF), in the early 2000s, FDEs had contributed approximately 6 percent of total national budget revenues. By 2013, the budget contribution of FDI sector

has reached to 15 percent. It should be noted that this figure is only calculated the direct contributions, such as corporate income tax, value added tax, national resource tax, import and export tax, etc... but do not included any other indirect contributions such as personal income tax of employees working in the FDEs. In addition, these contributions are also excluded revenues from oil exports of the FDEs. However, the contribution to the budget of the FDI sector is not too impressive compared to the other two economic sectors. Part of the reason is because the FDEs receive a lot of tax incentives to invest in Vietnam. There is also another reason that many FDEs have signs of transfer pricing, especially for multinational enterprises.

Figure 14: Contribution of the FDEs on tax revenues and exports



Source: Vietnam GSO and MOF

In addition, the FDI sector has contributed significantly to the success of Vietnam's exports, helping to improve the status of trade balance and increasing foreign reserves. GSO's figures show that in the mid-1990s, the proportion of export value of the FDI sector had accounted for an average of 30-percent of the total value of exports for the entire country. In recent years, while the economy fell into a recession and the health of the domestic economic sectors became difficult, the FDI sector continued to hold the engine of growth for Vietnam's economy, particularly in the area of exports archievement (FETP 2013). In 2013, the share of exports of FDEs increased 2.5 times compared with 20 years ago and is expected to grow in the coming years.

5.5. Labor and employment

Economic growth and job creation are the top priority objectives of the Vietnamese Government. So far, the Vietnamese Government has set the tasks for the public sector. In fact, the ability to create new jobs of the SOEs is very low, but tends to decrease. Meanwhile, the current distribution of FDEs into the labor market are relatively modest, only about 3.4-percent of the total labor force working annually during the period 2007-2012, but this proportion significantly improved compared with the 1.9-percent of the period 2001-2006 and with 0.7-percent of the period of the mid-1990s. In 2013, the number of employees working in the FDI sector was approximately 1.8-million and accounted for 3.4-percent of the total number of employees working in all economic sectors.

Above and beyond the number of direct jobs created by the FDEs, this sector also created indirect jobs in the service sectors and in the supporting industries in Vietnam through the cooperative relationships and links between foreign firms and domestic firms (CIEM 2006). According to Vietnam's Ministry of Planning and Investment (MPI), the indirect jobs created by FDI companies total approximately 3-4-million laborers. Laborers attracted to work in the FDI sector have contributed to the trend of the labor structure shift in Vietnam towards industrialization.

Employees working in the FDEs are also quite diverse and consist of unskilled to highly-technical laborers. A positive spillover effect for laborers working in FDEs is that they are learning by doing things relating to business management, new prodution methods, exposure to modern technology, formation of labor discipline, and practice of industrial styles, etc. After working in FDEs, laborers move outward and form their own businesses, become self-employed, and use the knowledge they learned to manage their business activities. These are the imporatant spillover effects that are generated by FDEs.

5.6. Technology Transfer

One of the main objectives of the strategy attracting FDI capital in Vietnam is to encourage technology transfer aiming to improve the technology level of Vietnam. Overall, the majority of FDEs use a lateral or higher level of technology with that of the local enterprises, and this level of technology is popular as in nearby countries (Dao Quang Thu 2013). According to the statistics from Vietnam's Ministry of Science and Technology (MOST), more than 951 technology transfer contracts have been registered since 1993, of which 605 contracts are from FDEs, accounting for 63.6 percent. Some industries have done a good job of technology transfer, such as petroleum, electronics, telecommunications, computer science, mechanical engineering, automotive, textiles, footwear, etc. Activities of FDEs in Vietnam have created the technological spillover effects through linkages in the business cooperation activities with domestic firms. In addition, based on the collaborative relationship with FDI firms, domestic firms have boldly invested and applied advanced technology into their business activities in order to meet the requirements of the cooperation and also to ensure the competitive position of domestic firms under the competing pressures of outside firms.

5.7. Improving the national competitiveness

Research conducted by Dao Quang Thu in 2013 was based on the criteria of capital, technology, management skills, the ability to access the market, and capacity to participate in global production networks to show that the competitiveness of the FDI sector is much higher than that of the domestic sectors. We may all know that one of the determinants of competitiveness of a country is productivity (Porter 2008). The production foundation of foreign enterprises is better than that of domestic enterprises, including SOEs (MPI 2013). Therefore, the involvement of the FDI sector has contributed to improving competitiveness for Vietnam's economy. This is reflected in the capacity to contribute to the annual exports turnover of the FDI sector as analyzed previously. Furthermore, the involvement of the FDI sector also arouses competitive motivation for domestic enterprises, especially for SOEs. To perform a key role, the Vietnamese Government always bestows privileges for SOEs. This policy has seriously distorted the business environment in Vietnam, especially when the private enterprises have always been treated unequally in terms of business opportunities. The involvement of the FDI, in some aspects and certain fields, helps break the monopoly of SOEs and thereby contributes to a more equal and competitive playing field between the economic sectors.

From the perspective of the state agencies, the involvement of foreign investors has forced policy makers to change their thinking on how to govern the economy, perfect the legal system, improve the openness and transparency in policy formation, apply the international standards and practices in the management and administration of the economy, and improve the competitive environment. Obviously, competition is good medicine to help improve the productivity and competitiveness of Vietnam's economy.

5.8. Some of the shortcomings and limitations of FDI in Vietnam

The above analysis shows that FDEs have significantly contributed to the achievement of economic growth in Vietnam, but there are still many limitations and inadequacies that prevent FDEs from developing as completely as expected.

Use of unskilled labor

One of the limitiations indicated is that the proportion of new jobs created by the FDI sector is still very low including a downward trend in the post-WTO period (2007-2012) (see Table 1). Overall, labor used by FDEs is mainly unskilled labor, which does not require too much skill and technical expertise. This is probably the trap of the policies to attract FDI in Vietnam as it is based on the advantage of cheap labor. The average income of employees in FDEs is higher than that of domestic private enterprises, but lower than that of SOEs. A survey conducted by the Ministry of Labor, Invalids, and Social Affairs (MOLISA) of Vietnam, released in March 2014, shows that in the fourth quarter of 2013 that the average monthly wage of workers in FDEs is about US $220.00 - higher than the wages of workers in the private sector (about US $213.00), but lower than that of workers in the SOEs (US $238.60).

The life of workers in FDEs as well as domestic businesses generally remains difficult. The demand for housing, daily life and cultural activities of workers in industrial zones are needed, but as of yet has not come to fruition. The number of labor disputes is increasing due to conflicts of interest between workers and employers. From 1995 to present, over 4,142 strikes broke out in which more than 75-percent is attributed to FDEs (approximately 3,122 cases) which were mainly associated with the FDI of Taiwan, Korea, China, and Japan.

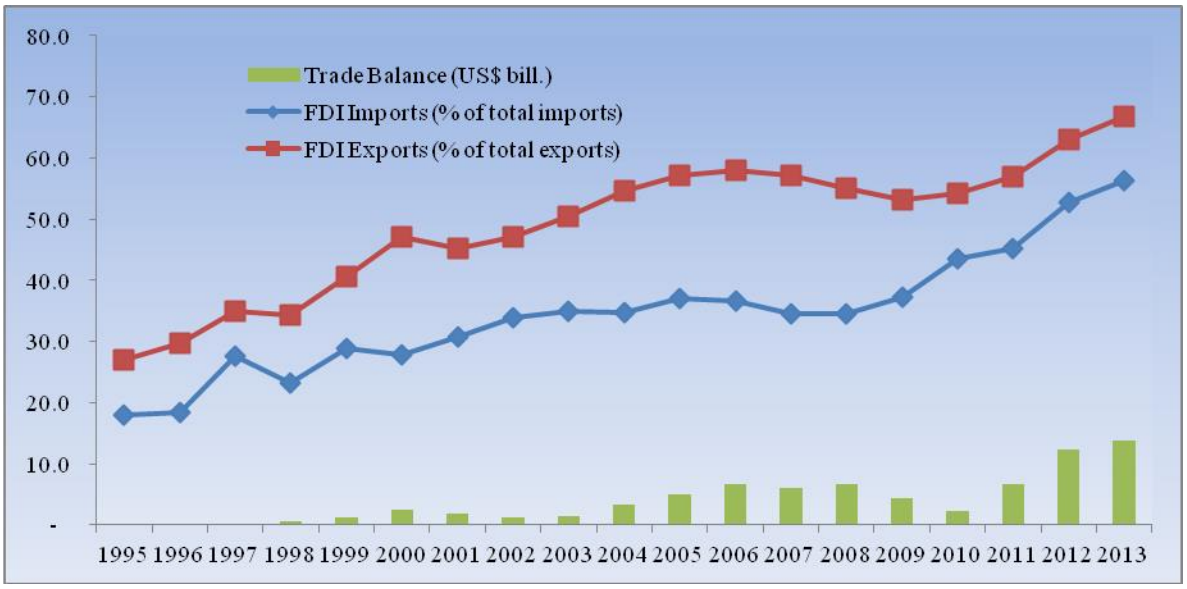
Mainly imports of inputs

As analyzed, export achievements, that FDEs created, are undeniable, but this sector also heavily imports raw materials for production. The proportion of imports of FDEs has increased significantly from 18-percent since the mid-1990s to over 56-percent in 2013. Fortunately, the FDI sector thus far is still a net exported sector, for example the surplus of trade balance in this sector has increased continuously since 2010, reaching nearly US $14-billion in 2013.

The high import demand of the FDI sector shows the limitations of Vietnam's domestic production rather than the weaknesses of FDEs themselves. FDEs did not find any local suppliers qualified to participate in their production chain. Clearly the Vietnamese enterprises have ignored the advantage of the so called geographic cost to participate as suppliers of inputs for FDEs in their own country. Succinctly, Vietnam has not built supporting industries developed enough to link with the value chain of FDEs. This is one of the shortcomings of the development policies for the supporting industries in Vietnam in previous decades, because it was not designed in a synchronous manner with the strategy of attracting FDI. Moreover, the policies to attract FDI in Vietnam do not provide proper motivation for foreign investors to

participate in the development of Vietnam's supporting industries. Finally, the macroeconomic policy, particularly the exchange rate policy, is also encouraging importing rather than building supporting industries in Vietnam.

Figure 15: FDI's Imports and Exports

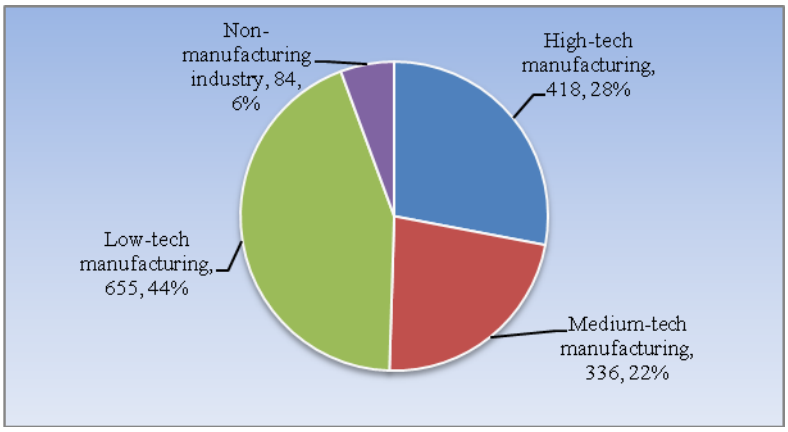


Source: GSO of Vietnam

Using outdated technology, environmental pollutions

The statistics of MOST (2013) shows that over 80 percent of FDEs use technology at the level of the world's average. Only 5-6-percent of enterprises use high-tech, and the remaining 14-percent are using technology at a low level and backwards. A 2013 report of MPI indentified that low-tech enterprises in Vietnam engage primarily in outsourcing. Some businesses are considered as high-technology, but the level of the use of high-tech is not implemented in Vietnam.

Figure 16: Sample distribution by type of manufacturing technology level



Source: UNIDO and MPI 2012

Consequently, Vietnam's enterprises now only produce low value added producst making it very difficult to participate in global production networks (MPI 2013)[4]. With the use of outdated technology the competitiveness of FDEs in Vietnam is not as high when compared with firms in other countries which have a higher level of technology. In addition, the use of outdated technology also causes high energy consumption and creates environtmental pollutions. This may be the result of the low energy price policy of the Vietnamese Government, such as power price, which inadvertently encourages businesses to import energy-intensive technology. Many people worry that Vietnam has the potential of becoming a "technology landfill" in the near future.

Transfer pricing and tax revenues issues

The percentage contribution to the budget of FDEs appeared to increase compared with the previous decade, but the overall contribution is still quite low compared to the expectations. This limitation is partly due to FDEs enjoying more preferential policies on income tax in the first period of investment in Vietnam and many other incentives. The findings of UNIDO (2012) argued that investment incentives are costly, distort the tax system, and limit state budget revenues. A probem emerged in recent years that many foreign enterprises have signs of transfer pricing in Vietnam. Obviously, transfer pricing is not a new problem and not only in Vietnam, but this problem is seriously being observed by the Vietnamse Government. A recent report from the Vietnam General Department of Taxation shows that transfer pricing in FDEs is complicated. In 2010, the Tax Inspectorate inspected 575 foreign enterprises and found that 43 enterprises had signs of transfer pricing. In 2011, the Tax Inspectorate also discovered that 921 foreign enterprises declared a loss and had signs of transfer pricing. In early 2014, resulting in 870 inspections of the General Department of Taxation revealed that up to 720 foreign enterprises violated tax policies in Vietnam.

A myriad of FDEs, especially transnational corporations, are involved in a suspected case of transfer pricing in Vietnam. In fact many FDEs haven't reported their lost operations in a long time, but continued to increase investment activities and expand their businesses in Vietnam. Transfer pricing is becoming more and more sophisticated and often bypasses tax professionals in Vietnam.

Inspection results also showed that the common method of transfer pricing used by FDEs is to increase inputs materials while lowering export output prices to create a financial loss in order not to succumb to the corporate income tax in Vietnam. Foreign enterprises in this category usually operate in the fields that have a lot of intangible assets such as patents, exclusive manufacturing formula or practices, and proprietary technology. So there are no appropriate criteria or benchmarks for comparison (Do Thien Anh Tuan 2014d). Transfer pricing behavior of foreign enterprises not only causes losses to the national budget, but also undermines the competitive environment of the economy.

Technology transfer restrictions

An evaluation conducted by MOST showed technology transfer activities in FDI projects have a positive contribution to the innovation and the improvement of technological capacity of Vietnamese enterprises. However, these activities have not yet met the requirements of the practice and the technological innovation needs of the whole of enterprises in the economy (MOST 2013). This is not necessarily due in part of the FDI, but mainly because the policy of encouraging technology transfer in Vietnam is

[4] See more at http://vinacorp.vn/news/thu-hut-fdi-hao-hung-hot-rac-cong-nghe/in-543564.

inadequate. Some shortcomings pointed out by MOST (2013) include: (i) the direction of attracting high technology has not achieved the expected results; (ii) the evaluation of technology is not given adequate attention; (iii) the reception and learning of new technology from FDEs is still weak. Although technologies transferred to Vietnam mostly have technological levels equal to the available technology in Vietnam, but on par with the average level in other countries. In addition, the technology transferred under the FDI projects is often based on the interests of the foreign investors, which do not necessarily fit the needs of technological innovation that Vietnam wishes.

5.9. The debate about the role of FDI in recent years in Vietnam

The above analysis argued that, after nearly three decades of reform and opening up the economy, FDI has contributed significantly to the economic growth in Vietnam, helped restructure the economy towards industrialization, strengthened the competitiveness of the economy and contributed to the annual export turnover, created a significant number of jobs and improved income levels of Vietnamese laborers. Many analysts point out, however, that compared to the expectations and goals of growth set by the Vietnamese Government, such as low contribution amounts in the labor market, limited tax contributions, the use of lower levels of technology, limited technology transfer, investment in resource-intensive industries, energy consumption and environmental pollution, loose links with local industry, etc. there are many inadequacies and limitations of FDI. For this reason, many people started criticizing the role of FDI, as well as Vietnam's FDI attracting policies. However, it is fair to say that the limitations of the FDI sector as analyzed are mainly due to the inadequacies of FDI attracting policies of Vietnam, as well as the weaknesses of domestic production rather than the FDIs themselves. For decades, the strategy to attract FDI in Vietnam has seen almost no changes in quality and mainly attracted as much FDI capital as possible without much emphasis on the quality of the project as well as the capacity of the investors.

The orientation of objectives pertaining to the industrialization policy of Vietnam have not been conducted clearly or comprehended completely, such as neglecting to identify the sectors in which Vietnam has competitive advantages from which to design policies to attract FDI accordingly. SOEs are always assigned to implement investment tasks based on subjective opinions of the government. Resources are then pumped into SOEs instead of reforming the investment environment, supporting and facilitating private sectors to help them participate in and compete together. Because of such policies, the benchmark of results of industrial policy in Vietnam is mainly generated by the SOEs sector, but this all too often characteristically the mark of failure (FETP/VELP 2013).

The critics of policies attracting FDI in Vietnam tend to focus on the incentives that the Vietnamese Government allocates to this sector. Furthermore, while the state sector always receives many incentives and privileges, the private sector receives almost no incentives at all. This has caused much controversy and criticism among Vietnamese economists. Table 1 demonstrates that the domestic private sector has a very large important contribution to every achievement of economic growth in Vietnam, while the resources used by this sector are very limited. With respect to the strategy of sustainable growth, it is imperative that Vietnam positively consider the advantageous role of this sector, however, countless obstacles on the policies and resources impede the development of the private sector and remain unresolved. Whereas, the Vietnamese Government continues to pump more incentives into FDEs and this causes even more controversy. In this context, many Vietnamese economists reconsider the role of FDI

and think of it in terms of the incentives and the contributions of this sector to the economy.[5] The purpose of their analysis is to expose the limitations of policies to attract FDI that Vietnam has been pursuing for so long. The analysis also argues that the economic growth of Vietnam in the future will not be sustainable once the domestic sector gradually fades as a result of not being able to compete in a policy environment that is increasingly less equal (see Bui Trinh 2014).

5.10. The institutional bottlenecks

The policy discussion paper of the Vietnam Executive Leadership Program (VELP 2013) argued that there have been reasons to slow down the economic growth in Vietnam in recent years. One reason is that the economy has been dependent on four separate engines of growth, most of which at present are doing poorly. The four engines of growth are the state-owned enterprise sector, the domestic private sector, the small-holder agriculture sector, and the FDI sector. Of these four engines, only the FDI sector continues to do well in large part because labor intensive FDI industries have begun moving out of China as wages there accelerate upward and because these enterprises are largely not affected by either the economic difficulties facing the Vietnamese economy or the weaknesses of Vietnamese institutions (VELP 2013).

An argument of VELP (2013) focuses on encountering the same, weak global economy and a structurally problematic domestic economy; domestic firms in Vietnam are still facing a lot of difficulties and even bankruptcy while FDI firms are continuing to grow. From a policy perspective, macroeconomic instability, high interest rates, and limited access to resources have negatively impacted domestic firms, while FDEs have somehow avoided these shocks.

However, from an institutional perspective, although FDEs have been established in Vietnam to make use of cheap labor, resources, and some policy advantages, this sector is still relying on external institutions to operate their businesses and production activities (VELP 2013). The legal system governing the contractual relationship of FDI firms is from the outside of the country. The model of corporate governance extends from overseas and is also the man in that model. Links in production are mainly with external firms and capital credit is also provided from foreign banks. Furthermore, interest rates paid by FDI firms are often less than local firms. In general, FDEs have "ignored" the majority of the institutions of Vietnam, which is considered to hamper business activities of enterprises in the country (VELP 2013).

The analytical approach of VELP (2013) argued that it is the institutional bottleneck that not only caused the short-term macroeconomic instability, but also created many obstacles for sustainable economic growth. These institutional weaknesses can help explain why Vietnam is still missing domestic supporting industries which are strong enough to supply inputs for the FDEs in Vietnam. Meanwhile, FDI enterprise's reliance on external institutions and avoidance of Vietnamese institutions explains why the foreign sector in Vietnam is not deeply rooted in the national economy. Strictly speaking, they do not have strong incentives to develop their linkages with domestic producers or help domestic supporting firms become part of their global supply chains. As concluded by VELP (2013), as long as Vietnam fails to develop effective market-supporting institutions which foreign enterprises can rely upon to expand their business activities, the current manufacturing process of low value added products based on imported inputs and domestic assembly will continue.

[5] See Bui Trinh (2013, 2014), Nguyen Mai (2014), Le Dang Doanh (2013, 2014), Nguyen Thi Tue Anh (2006, 2008), Do Thien Anh Tuan (2014c) and many other authors for more arguments.

6. Conclusion remarks

Despite some debates about the contribution of the FDI sector in Vietnam, the strategic economic reforms pursuing Vietnam should not fail to consider the role of this sector. The FDI sector will undoubtedly continue to be the driving force for economic growth in Vietnam, at least in the short-term when the obstacles of development of the domestic sector are still unresolved and the weaknesses of the state sector have not yet been processed.

The limited contributions of the FDI sector must be considered as the institutional bottlenecks in the domestic economy instead of viewing it as the responsibility of the FDI sector. In some ways, like the domestic enterprises sector, the FDEs can sometimes be victims of such weaknesses. The incentives that the Vietnamese Government gives to the FDI sector may be partially offset by these weaknesses, but the domestic private sector may not enjoy the fruits of these incentives.

The current economic reforms of Vietnam are are looking forward to the completion of a new institutional foundation, but there are many obstacles have made the implementation always be delayed. Many people are eagerly awaited the events that Vietnam would joint the TPP Agreement and see it as a boost to help Vietnam "take off" or to motivate Vietnam to reform its economy. However, lessons from the WTO accession in 2007 showed that such reforms should have gone a step ahead for the economy could keep adapting. The capacity of the state apparatus must be upgraded to meet new requirements of the integration. What expected from this economic reform is a fair competitive environment among the economic sectors, not only between the state sector and private sector but also between the foreign sector and the domestic private sector./.

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