

## Foreign Direct Investment in Vietnam — Awareness and Practical

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**Abstract:** In the process of industrialization and modernization of the country, foreign direct investment is considered as one of the important factors, contributing significantly to economic growth and restructuring of Vietnam. The foreign-invested business sector increasingly asserts an important role, positively contributes to economic growth, improves the balance of payments, and creates jobs for workers. At the same time, this area also creates a driving force to promote technology innovation, improve business management methods, enhance competitiveness and promote the process of economic restructuring in Vietnam in recent years.

**Key words:** foreign direct investment; economic restructuring; industrialization; modernization

**JEL code:** P2

### 1. Place the Problem

The view on the economic sector with foreign investment has gradually been formed and developed from the VI Congress of the Communist Party of Vietnam (1986) until now and the term “foreign invested economy” was first confirmed by the Communist Party of Vietnam at the IX Congress (2001), the XI Congress (2011) and the XII Congress (2016). Accordingly, the economy of foreign investment or foreign direct investment (FDI) is understood as the form of investment in which the foreign investor invests all or the majority of the investment capital of the project to win the right to operate or participate in operating the manufacturing or service business.

The Marxist-Leninist theory affirms that the existence of a foreign-invested economy is an objective inevitability in the period of transition to socialism and the transformation of this economic component is a basic, long-term economic missions of the whole transition period. The reality of Vietnam also shows that the development of this economic component in a socialist-oriented market economy is a right and consistent policy of the Party based on science, in accordance with regulations. Objective economic law, is the creative application of Marxism-Leninism, Ho Chi Minh's thought to specific historical conditions of Vietnam.

This theory becomes even more correct for Vietnam when in recent years, FDI has been one of the driving forces behind Vietnam's development, economic restructuring and international integration, which has achieved very satisfactory results.

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## **2. The Communist Party's Perception Process on the Economic Sector With Foreign Investment in the Doi Moi Era**

At the VI Congress (1986), the Party affirmed: “Announced policies to encourage foreign investment in our country in many forms, especially for industries and facilities requiring high technology, making export goods. Along with the announcement of the investment law, there should be policies and measures to create favorable conditions for foreigners and overseas Vietnamese to enter our country for business cooperation” (Communist Party of Vietnam, 2005). However, encouraging foreign investment, the Party also noted: “The expansion of external economic relations will create complicated problems, it is necessary to take measures to limit and prevent negative phenomena, but it was not so that the door closed” (Communist Party of Vietnam, 2005).

The VII Congress of the Party (1991) advocated: “taking advantage of all possibilities and using many forms of attracting foreign capital” with the aim of “breaking the siege, economic embargo against our country” and “to attach importance to the form of foreign companies investing directly in our country, associated with the transfer of advanced technologies and boosting exports” (Communist Party of Vietnam, 2005). To implement this policy, the Party affirmed the need to: create favorable environment and conditions for foreigners to enter our country for investment and business cooperation. Institutional development is synchronous, stable, convenient and strictly implemented; unify the focal point to settle foreign investment procedures and requests. Ensure essential infrastructure, working and living facilities for foreigners, first of all, export processing zones and focal areas in external economic relations. To organize well economic information and proactively prepare projects calling for foreign investment capital. Train staff to meet the requirements of foreign economic activities under the new mechanism, with new subjects (Communist Party of Vietnam, 2005). However, the Party also noted that the encouragement of foreign direct investment must be placed in the development strategy and synchronous management mechanism, ensuring the sovereignty, the ability to control and the direction of the State over the process socio-economic development process. Developing state management mechanisms for the implementation of foreign-invested investment projects and completed construction works in operation, coupled with the expansion of many forms of investment, should gradually increase share of Vietnamese participation in joint venture cooperation (Communist Party of Vietnam, 2005).

Until the VIII Congress (1996), the Party continued the policy of “increasing the ability to receive investment capital and technology from the outside” with specific tasks and solutions: foreign direct investment (FDI) is aimed at sectors, products and services with advanced technology, with a high proportion of exports. For industries that do not require a lot of capital and high technology, and can profit quickly, they must use many forms to mobilize domestic capital to invest entirely or occupy a high rate of capital contribution if joint venture is required. Regarding the investment area, it is necessary to have effective policies and measures to attract potential places but still face difficulties. The form of investment should continue to diversify, pay attention to new forms, such as financial investment (outside capital contribution, share purchase, but not participating in management like joint venture enterprises). Regarding investment partners, it is necessary to strengthen cooperation with multinational companies to take advantage of source technology, approach modern management methods and quickly penetrate into international markets and expand new market (Communist Party of Vietnam, 2005). With this policy, the Party has initially experimented with allowing companies and foreigners to buy shares of domestic joint-stock companies, including equitized state-owned enterprises, within the limits set by business lines.

The IX Congress (2001) — The first Congress of the Party conducted in the new millennium - identify our country's general economic model during the transition to socialism as a socialist-oriented market economy and affirm the socialist-oriented market economy means “a type of economic organization that both obeys the laws of the market economy and is based on and is led by principles and nature of socialism” (Communist Party of Vietnam, 2005). On the basis of the socialist-oriented market economy, with the foreign investment economy, the Party determined: “The foreign-invested economy is a part of the Vietnamese economy and encouraged to develop, focusing strongly on the production and trading of exported goods and services, high-tech goods and services, and building infrastructure” (Communist Party of Vietnam, 2005). On the basis of the socialist-oriented market economy, with the foreign investment economy, the Party determined: “The foreign-invested economy is a part of the Vietnamese economy and encouraged to develop, focusing strongly on production and trading of export goods and services, high-tech goods and services, and construction of infrastructure” (Communist Party of Vietnam, 2005). Thus, the economic sectors of foreign investment have been separated from the city part of the state capitalist economy to become an independent economic sector in the socialist-oriented market economy in Vietnam.

Summarizing the 5-year implementation of the Resolution of the IX Congress, for the foreign-invested economic sector, the Party's Congress X (2006) assessed: “the foreign investment economy has a relatively high growth rate, accounting for 15.9% of GDP, is an important bridge to the world in technology transfer, international trade” (Communist Party of Vietnam, 2006), with the important contribution of this economic component to the in recent years, the Vietnamese economy continued to affirm that foreign-invested enterprises are an important part of the Vietnamese economy and are treated equally as Vietnamese enterprises in doing business. Create favorable conditions for foreign investment to participate more in the development of industries and territories in accordance with our country's international commitments (Communist Party of Vietnam, 2006).

With the important contributions and position of the foreign investment economic sector since it was identified (2001), the National Construction Platform in the period of transition to socialism (addition, development year 2011) emphasized: “foreign investment economy is encouraged to develop” (Communist Party of Vietnam, 2011) and at Congress XI (2011), the Party determined: must “attract the resources of the foreign investment “in the form of” improving the legal and economic environment, diversifying forms and mechanisms to attract foreign investors' resources into important business sectors and fields” (Communist Party of Vietnam, 2011) and “attracting foreign investment with modern technology, friendly with the environment and strengthening links with domestic enterprises” (Communist Party of Vietnam, 2011).

After more than 30 years of the Law on Foreign Investment officially passed (1987), with positive results from FDI, the XII Congress of the Party (2016) has made a policy to continue attracting FDI in the future: “Reviewing and amending laws and policies to strongly attract foreign investment, especially projects with high technology, environmental friendliness, value added products and high localization rate, joining global production networks and value chains to promote economic restructuring. To increase the attraction of foreign investment with high technology, environmental friendliness and labor intensive use. Encourage investment in the construction of infrastructure and supporting industries, renewable energy, new materials, electronics, information technology, biotechnology, plant varieties, livestock, artificial training resources and high-quality health care,... There are flexible incentives for specific projects. Encourage the establishment of research and development centers for foreign-invested enterprises in Vietnam” (Communist Party of Vietnam, 2016).

### **3. Foreign Direct Investment Gradually Affirms Its Role and Position in the Process of Development and Economic Restructuring of Vietnam.**

Under the impact of the open door policy, it has become one of the main factors contributing to the rapid economic growth of Vietnam. Among the factors contributing to Vietnam's growth in recent years, FDI is one of the important factors. On the other hand, FDI is also an important factor that has recently contributed to accelerating the process of economic restructuring in Vietnam.

Over the past time, the role and position of FDI in the Vietnamese economy has been increasingly confirmed. Specifically:

In the period 2006-2011, according to the General Statistics Office, as of December 31, 2011, there are 9,010 FDI enterprises in operation. In which, 100% foreign-owned enterprises are 7,516 enterprises (accounting for 83.4% of all FDI enterprises), joint-venture enterprises are 1,494 enterprises (accounting for 16.6% of all FDI enterprises) with total the number of employees working in FDI enterprises is more than 2.5 million people, of which 100% foreign-owned enterprises account for 89.7%, and that of joint ventures with foreign enterprises is 10.3%, on average each year attracted 221 thousand workers, significantly contributing to job creation and increased income for workers (General Statistics Office, 2014).

By the end of 2011, foreign investment remained the fastest growing sector among economic sectors with GDP growth higher than the GDP growth rate of the whole economy. The growth rate of GDP in 2011 compared to 2010 of the FDI sector increased by 6.30% while the GDP of the whole economy increased by 5.89%. Thus, as of 2011, after more than 20 years of operation, FDI enterprises have become an important part of the entire Vietnamese enterprise, accounting for 16.1% of capital for production and business; 18.3% of fixed assets; 19.7% of total revenue; 31.5% of profit before tax; 32.2% contributed to the State budget (General Statistics Office, 2014).

Thus, in the 2006-2011 period, foreign investment promotes structural transformation towards industrialization and modernization. Foreign investment focused mainly on industrial production. The growth rate of the industrial FDI sector reached an average of nearly 18% per year (General Statistics Office, 2014), higher than the growth rate of the whole industry. In this period, the FDI sector created nearly 45% of the production value of the whole industry, at the same time contributed to forming a number of key industries of the economy such as telecommunications; oil and gas exploration, exploitation and processing; manufacture of electronic products; information technology; steel, cement production.

For the average income per employee per month in 2011 of FDI enterprises was 4.94 million VND, 2.3 times as much as in 2006. In the form of investment, joint venture enterprises have higher income, achieving VND 6.8 million, approximately 2 times higher than 2006, while the average income of workers in the 100% foreign-owned sector was 4.78 million VND. By economic sector, the service sector achieved the highest average income with 12.8 million VND, 2.3 times as much as in 2006. Industry and construction sector followed by 4.4 million VND and low especially the agriculture, forestry and fishery sector with 4.3 million dong (General Statistics Office, 2014).

In the period of 2011-2016, FDI continued to assert its position and role in the process of economic development and restructuring of Vietnam. Specifically:

The FDI sector has positively contributed to the gross domestic product (GDP) with its contribution

increasing over the years<sup>1</sup>, always being the most dynamically developed area of the economy<sup>2</sup>, and an important part of the whole country Vietnam business sector ministry. By the end of 2016, although the number of FDI enterprises only accounted for 2.8% of the total number of enterprises in the country, it accounted for 18.1% of the capital for production and business; 18.5% of fixed assets and long-term investments; 27.4% of net revenue; 45.9% of profit before tax and 29.1% of contribution to the State budget (General Statistics Office, 2018).

The FDI sector promotes economic restructuring in the direction of modernization, is an important factor promoting the development of many new industries and products, contributing to the formation of some key industries of the economy such as: oil and gas, electronics, information technology, cement, steel ..., increase the production capacity of the economy. In the service sector of Vietnam, FDI has created many high quality services, such as banking, insurance, auditing, shipping, logistics, hotels ..., step by step creating favorable conditions for the market development services and increase international economic integration.

Through FDI, Vietnam has access to advanced technology of the world to develop economic sectors using modern technologies, such as: biotechnology, post and telecommunications, software industry, electronics ... Many new technologies have been transferred, creating an important turning point in the development of a number of key economic branches of the country, such as: oil and gas; telecommunication; electronic; textile; leather shoes.

Over the past years, the FDI sector has contributed to improving Vietnam's export capacity, becoming a bridge and good conditions for Vietnam to quickly approach and cooperate with many countries, contributing to step by step improvement. Vietnam's position and power in the context of globalization. Exports from the FDI sector accounted for over 66% of Vietnam's total merchandise exports on average in the 2011-2016 period<sup>3</sup>. In addition, FDI enterprises also contribute to stabilizing the domestic market, limiting trade deficit through providing the domestic market with high quality products produced by domestic enterprises.

The FDI sector also contributes to creating many jobs for workers. In 2016, nearly 4.2 million jobs were created, 1.6 times higher than in 2011. The on-site training and the training outside of the FDI sector are especially focused, in order to improve workers' qualifications, technicians, officials. A part of the trained labor force has managerial capacity, scientific and technological qualifications that can replace foreign experts, these are the nucleus for developing a highly qualified and skilled workforce of Vietnam.

It can be said that, thanks to the important contribution of the FDI sector, Vietnam has achieved high economic growth over the years, known as a dynamic, innovative and attractive country received the attention of the international community, clearly demonstrating the important role of FDI in the success of Vietnam's innovation policy.

Thus, the business efficiency of FDI enterprises has increased significantly over the years. The profit margins of most businesses have been significantly improved. The rate of return on capital of the entire FDI sector increased faster than that of other regions. These results have contributed significantly in the process of economic restructuring in Vietnam over the past time.

<sup>1</sup> The proportion of the FDI sector contributes to GDP, in 2011: 15.66%; 2012: 16.04%; in 2013: 17.36%; 2014: 17.89%, 2015: 18.07%, 2016: 18.59%.

<sup>2</sup> The GDP growth rate of the FDI sector is always higher than the national GDP growth rate. In 2011: GDP of the FDI sector grew by 7.69% while that of the whole country grew by 6.24%; in 2012: this rate was 7.42% and 5.25% respectively; in 2013 it was 7.86% and 5.42%; in 2014 it was 8.45% and 5.98%; in 2015 it was 10.71% and 6.68%; in 2016 it was 9.55% and 6.21%.

<sup>3</sup> In 2011, it accounted for 56.9%; in 2012 accounted for 63.1%; in 2013 accounted for 66.8%; in 2014 accounted for 67.4%; in 2015 accounted for 70.6%; in 2016 accounted for 71.5%.

In short, since the Law on Foreign Direct Investment was passed (1987), FDI inflows have always been an important driving force in our country's socio-economic development during more than 30 years of renovation. Especially in the recent period, Vietnam is stepping up the process of economic restructuring and proactive international economic integration in an increasingly strong globalization environment.

In addition to the above positive results, the FDI sector in recent years still reveals a number of shortcomings and limitations, including:

Firstly, FDI enterprises mainly focus on processing and assembling, raw materials are mainly imported, so the added value is not high, typically the assembly activities of automobiles, motorcycles, and electricity - electronics, garment, footwear, while Vietnam is a country with advantages in agriculture, the share of FDI enterprises' investment in agriculture is very low and increases very slowly<sup>4</sup>.

Second, the great expectation of Vietnam is that FDI enterprises will actively contribute to the transfer of advanced technology, improve qualifications, experience and skills for Vietnamese business managers. At the same time, to rapidly develop industries with high technology, create many added values, and help accelerate the process of industrialization and modernization of the country. However, the results achieved are still limited and inadequate. As of December 31, 2016, the proportion of enterprises with 100% foreign capital was 11,974 enterprises, accounting for 85.5% (General Statistics Office, 2018) (the remaining 14.5% were joint venture enterprises with foreign countries), while the current FDI enterprises mainly focus on operating in industries, sectors that use a lot of unskilled workers have low labor costs. Although foreign investment in Vietnam has been over 30 years, the investment of other countries is still mainly focused on the processing and manufacturing industry, exploiting oil and gas, but until now, almost Vietnamese industry is still there is no manufacturing and processing industry of high technology, employing a lot of skilled and highly skilled labors, creating a lot of added value, mainly enterprises engaged in outsourcing activities assembling with normal or outdated equipment and production lines.

Third, the proportion of FDI enterprises doing business with losses tends to increase<sup>5</sup>, the number of jobs created is not much<sup>6</sup>, the life of workers in FDI enterprises is not adequate.

The average monthly income of workers in the FDI sector in 2016 was 8.5 million VND/month, only higher than the income of non-state enterprises (6.4 million VND/month) but much lower with the average income of employees in the State-owned enterprises sector (11.4 million VND/month) (General Statistics Office, 2018).

Fourth, a number of projects have been licensed but have not yet ensured their sustainability, caused environmental pollution, consumed energy and resources, and have not paid enough attention to national security.

Vietnam's environmental regulations apply the standards of developed countries, but the appraisal is only superficial, focusing much on the pre-check stage, leading to many projects that when implemented, seriously violate the regulations on the environment, causing long-term impacts to the health of the people and the regional ecology. Many projects to import outdated machinery and equipment causing environmental pollution have not been detected in time. There is a tendency to shift foreign investment that consumes energy and resources, human resources, and is not environmentally friendly into Vietnam, but many localities do not have an environmental control mechanism. Some projects have taken up large land but have not implemented, causing waste of resources.

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<sup>4</sup> In 2014, FDI in agriculture was 0.5%, 2015 was 1%, 2016 was 0.4% and 2017 was 1.1%.

<sup>5</sup> It was 47.7% in 2006, 45% in 2011, 47.9% in 2016.

<sup>6</sup> As of December 31, 2016, there were nearly 4.2 million employees working in FDI enterprises, accounting for 29.6% of the total number of employees working in various types of enterprises.

Some cases of investment attraction have not taken into account the overall effectiveness of national defense, especially afforestation, mineral exploitation, aquaculture and aquaculture projects in areas sensitive to security and national defense. Some projects use a lot of foreign unskilled workers.

Fifth, there is the phenomenon of transfer pricing and tax evasion.

Some foreign-invested enterprises have shown signs of applying sophisticated transfer pricing techniques such as shortening the value of capital contribution (by machinery, equipment, copyright ...), the purchase and sale of raw materials, semi-finished products, finished products, services, management fees, royalties, guarantee costs, loans, salary payment, training, advertising, contractors, capital transfer... create “fake losses, real profit”, causing loss of budget revenue, making the majority of Vietnamese parties have to withdraw from the joint venture, the enterprise becomes 100% foreign capital.

#### 4. Conclusion

With specific contributions to economic growth, generating budget revenue, creating jobs and promoting economic restructuring, international integration, it is clear the important role of FDI in development socio-economic development of Vietnam. However, in addition to its positive role, FDI has also created many negative problems for the economy, such as polluting the environment, rampant exploitation of natural resources, and importing outdated technology, avoiding financial obligations. These limitations have made the efficiency of using FDI in the economy low and unsustainable.

In the new development context of Vietnam, FDI still plays an important role in the process of industrialization, modernization, economic restructuring and international integration. However, the role of FDI is only really enhanced if it is used effectively and creates sustainable development. Therefore, attracting and using FDI selectively, encouraging investment in industries that the economy really needs and developing in accordance with the orientation of economic restructuring, ensures sustainability long-term attention should be paid in the future.

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