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Sudden Surge in FDI and Infrastructure Bottlenecks
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Through examining trends and patterns of foreign direct investment (FDI) in Vietnam over the twenty years of reform (1986–2008), this paper found a big increase in registered FDI recently. This is not in accordance with the increase in actual capital disbursement because of low absorptive capacity of the economy in terms of poor infrastructure, restricted and unstable policy, and weak competitive capacity of domestic firms. Moreover, newly massive flows of FDI brought an explosion to infrastructure development in the form of office buildings, hotels, industrial zones, resident parks and ports. This could help to improve the situation of infrastructure because it has not kept pace with the rapid economic growth over the past decade and are considered as major constraints in attracting more FDI.

Keywords: Vietnam, foreign direct investment (FDI), mergers and acquisitions (M&A), entry mode, infrastructure.

I. Introduction

During the reform period (initiated since 1986), Vietnam has already achieved notable success in attracting FDI, and it has become an important component in gross national investment. By 2008, foreign-invested sector accounted for about 25 per cent of total gross domestic investment in the Vietnamese economy. Foreign invested enterprises (FIEs) have begun to make a significant contribution to employment generation and export expansion. The impressive economic outcome of FDI participation in the economy served to strengthen government commitment to further bring in reforms to improve Vietnam's attractiveness to foreign investors, particularly in export-oriented manufacturing.

The main objective of this paper is to investigate the roots of sudden increase in FDI inflow and patterns of FDI in Vietnam over the past two decades of reform with emphasis on investment area/sectoral composition. The causes and possible impacts of the increase in FDI on infrastructure development will also be carefully examined. This paper is based on data compiled from administrative records of Vietnam's Ministry of Planning and Investment (MPI) and other important databases on FDI (UNCTAD, CEIC and ASEAN FDI databases).

The structure of this paper is as follows. Section II reviews the impact of policy change on FDI inflows in Vietnam. This is followed by a discussion on the changes in the form of investment and patterns of source country. Analysis of FDI by investment area will be presented in section V. In addition, this paper assesses the geographical distribution of FDI in Vietnam with the premise of conventional classification of seven regions. Short conclusions on trends and patterns of FDI in Vietnam will be presented in the last section.

II. Policy Change and Sudden Surge in FDI Inflows

A Law on Foreign Investment was approved by the National Assembly just one year after the reform was launched in 1986. This law was amended five times in 1990, 1992, 1996, 2000 and 2003. The appearance and amendment of this law have contributed to the Reform (*Doi Moi*) policy of Vietnam. It was highly appreciated by the international community as an open, attractive law and was in line with international norms. Besides, over fifty bilateral and multilateral agreements related to FDI were also approved in order to encourage and protect foreign investors given the existing imperfect market mechanism in Vietnam.

The most important change in FDI policy was the approval by the National Assembly of two new laws — Investment Law and Law on Enterprises in December 2005. This reform aimed to create a consistent legal system as well as to set up a common playground for three main players: FIEs, state-owned enterprises (SOEs) and domestic private enterprises (DPEs). The new Investment Law has some main benchmarks. The first is the new law replaces two separate laws — the FDI Law and the Law on Domestic Investment Promotion. Therefore, all kinds of investment are treated in the same way. The second significant feature is reduction of paperwork involved in FDI approval/monitoring and the response time for issuing an investment certificate. The third one involves strong decentralization on approving and licensing FDI projects to the provincial people committee and the management committee of industrial zones/export processing zones (IZs/EPZs). Lastly, all regulations related to FIE establishment and operation were separated from the Investment Law. Alternatively, these firms will be governed by the new Law on Enterprises as other firm types.

The data on FDI inflows have been inconsistently published among different census organizations. There is a significant difference between the data published by Vietnamese government agencies and the data from international organizations. For example, Table 1 compares FDI inflows from three different sources: MPI, UNCTAD and the General Statistics Office of Vietnam (GSO). MPI is a legal administrative body for managing FDI and Official Development Aid (ODA). The difference among data sources stems from the method of measuring FDI. MPI defines FDI as total investment in FIEs and, therefore, includes shares of capital from both domestic and foreign partners. A change in the FIE capital stock as a result of earnings invested is also regarded as a change in FDI. Meanwhile, most international organizations, like UNCTAD define FDI by two types of investment: Greenfield investment measured by the actual capital inflows from multinational enterprises (MNEs) and cross-border merger and acquisition (M&A) activity. This mostly explains why MPI figures on realized investment[1] are much bigger than those in the UNCTAD source. Another reason for the difference originates from the capability of the statistical agency in identifying FDI. Until 2003, FDI data in Vietnam did not cover either reinvested earnings or M&A. Table 1 also demonstrates some discrepancies in data from two government agencies (MPI and GSO), especially for the initial stage of capital flows. There are two possible reasons for this: difference in the time of reporting data, and inconsistency in data compilation between government bodies. Investment of Vietnamese people who are citizens of overseas countries (*Viet kieu)* is generally

TABLE 1
Registered and Realized FDI Flows to Vietnam by Sources of Data
(In US$ million)

Year	FDI flows, MPI source			Actual FDI flows, UNCTAD source	FDI flows, GSO source		
	Number of licensed projects	*Registered capital*	*Realized capital*		*No. of licensed projects*	*Registered capital*	*Realized Capital*
1988	38	322	—	8	38	322	—
1989	68	526	—	4	68	526	—
1990	108	735	—	180	108	735	—
1991	151	1,284	428	375	151	1,292	329
1992	197	2,077	575	474	197	2,209	575
1993	274	2,829	1,118	926	274	3,347	1,018
1994	367	4,262	2,241	1,945	367	4,535	2,041
1995	408	7,925	2,792	1,780	408	7,699	2,556
1996	365	9,429	2,923	1,803	387	9,735	2,714
1997	348	5,822	3,218	2,587	358	6,055	3,115
1998	275	4,781	2,375	1,700	285	4,877	2,367
1999	311	2,197	2,537	1,484	311	2,264	2,335
2000	379	2,494	2,420	1,289	389	2,696	2,414
2001	550	3,236	2,430	1,300	550	3,230	2,451
2002	802	2,805	2,591	1,200	802	2,963	2,591
2003	772	3,128	2,650	1,450	748	3,146	2,650
2004	723	4,222	2,860	1,610	723	4,222	2,852
2005	922	6,339	3,300	2,020	—	—	—
Total	**7,058**	**64,413**	**34,458**	**22,135**	**6,164**	**59,853**	**30,008**

NOTE: — data not available.
SOURCE: GSO website, MPI database (various source) and UNCTAD database on website.

excluded from the official record on FDI because most of this investment is undertaken through their relatives who are Vietnamese residents.

Evidence from the ASEAN Secretariat and UNCTAD shows FDI inflows began before 1986 — the first year of reform initiated by the VI Communist Party Congress. However, most foreign investment in the planned economy phase was composed of official aid from governments of the former Soviet-bloc countries. Therefore, the entry of FDI was recognized as soon as a new law on FDI was sanctioned and became effective in 1987. Twenty years of attracting FDI can be divided into several episodes. In the first four years (1988–91), FDI inflow was small and affected by the internal instability of the economy (for instance, hyper-inflation and food shortages), and the collapse of the Soviet federation as well as the socialist countries bloc. At this stage, many restrictions and consequences of the planned economy prevented FDI inflows. A significant increase in FDI had just occurred when many FDI-related policies changed in accordance with stabilizing macro economic problems by the end of 1991. The next period (1992–97) witnessed continuous massive FDI inflows reaching a peak in 1996 with registered and realized capital at US$8.2 billion and US$2.9 billion, respectively (FDI data on the MPI website in 2006). FDI inflow then slowed as a result of the Asian financial crisis until 2000. A recovery period of FDI inflow began slowly from 2001 due to the cautious behaviour of foreign investors following the crisis. For instance, although reform had been extended further, registered capital for 2005 was considerably lower than in 1996. Fortunately, inward FDI seems more reliable as the ratio between realized capital and registered capital in 2005 was higher than 1996.

The fundamental reform of FDI-related policy in late 2005 has caused a sudden increase of FDI in recent years. Table 2 shows registered FDI in three years (2006–2008) was about five times in comparison with the previous period (2001–2005) and equivalent to 150 per cent compared with the total FDI of all years from 1988 to 2005. The data also demonstrate a large amount of realized capital in the past three years (US$23.6 billion). However, there was a big gap between the FDI commitment and actual disbursements in the last period (2006–2008) compared with the previous ones. The decreasing ratio of realized over registered capital in the last period is explained by the following reasons. Some provinces did not issue investment licences and business certificates accurately because they wanted to encourage FDI as much as possible. Consequently, there were some projects aiming to invest in the same field while the local demand is inadequate. Moreover, the national industry plan is not in line with the local plan, so the hand-over of land to foreign investors was difficult. The weakness in infrastructure (electricity, water, roads, and ports) is also a major obstacle to the disbursement of FDI. Besides, the shortage of trained workers, especially technical workers and engineers, causes the flight of foreign investors even though the wage rate in Vietnam is relatively competitive. Lastly, there were some big projects in infrastructure development (highways, ports, bridges, railways, hydro power) but they have not been implemented because of negative effects from the 2008 global financial crisis.

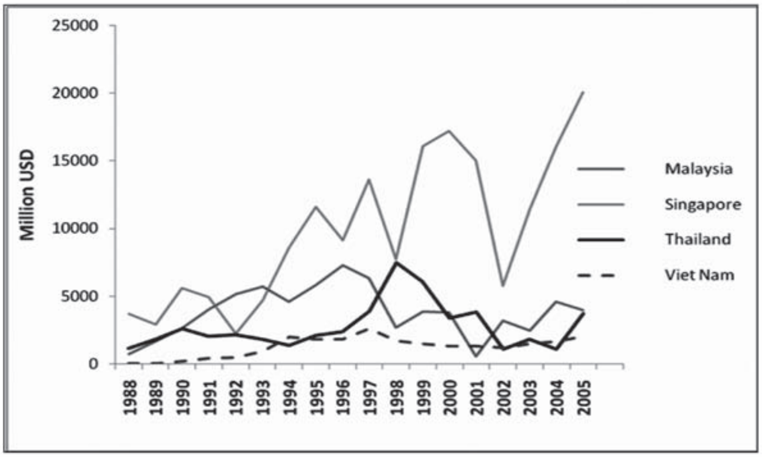
In comparison with selected host countries in the same region, this study uses common comparative indicators as employed in the World Investment Report produced by UNCTAD. The trends of FDI flows in Vietnam, Malaysia and Thailand are mostly the same, i.e., flows increased until 1997/1998 and decreased afterwards (Figure 1). However, the flow of this type of capital in Vietnam has been more stable than in the other two countries. Flows to China and Singapore seemed not to have been affected by the financial crisis and reached an extremely high level compared with other countries. For the whole period (1988–2005), FDI flows in Vietnam were far below the levels in other ASEAN countries. However, over the past four years, the values of

TABLE 2
FDI Inflows by Sub-periods
(In US$ million)

Periods	*Number of licensed projects*	*Registered capital*	*Realized capital*	*Realized/registered capital (%)*
1988–1990	214	1,583	0	—
1991–1995	1,397	18,377	7,154	38.93
1996–2000	1,678	24,723	13,473	54.50
2001–2005	3,769	19,730	13,831	70.10
2006–2008	3,702	97,362	23,636	24.28

SOURCE: Compilation from MPI database on website <www.mpi.gov.vn> (various sources).

FIGURE 1
FDI Inflows in Vietnam and Selected Host Countries
(In US$ billion)



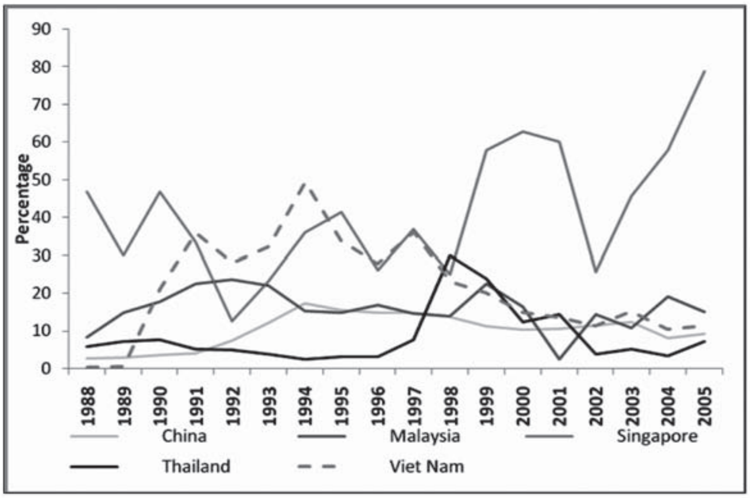
SOURCE: UNCTAD FDI database online, 2006.

these capital flows in Vietnam and Thailand have been mostly similar.[2] The gap between Vietnam and other countries may be explained by the difference in improving the investment climate. Despite these other countries previously having some reservations about the benefits of FDI, they all rapidly developed favourable environments for FDI from the early 1980s. However, Vietnam remained hesitant about reforming the investment climate. The long-lasting effect of the Asian crisis in Vietnam compared with the other nations is a typical example of factors causing the sluggish change in policy to overcome negative externality. After the crisis, many ASEAN countries introduced additional incentives and more aggressive investment promotion programs (JICA 2003), whereas the fundamental policy changes in Vietnam have occurred only recently. Vietnam has so far had two main forms of foreign investment — joint ventures and fully-owned FIEs. Apart from these entry modes, other nations have received more capital from encouraging M&A and any other forms of investment, so that the total capital going to these countries is more volatile than that going to Vietnam.

Country comparison by other indicators, such as shares of FDI flows in gross fixed capital formation (GFCF) and the FDI flow/GDP ratio, shows different trends (Figures 2 and 3). The FDI share in GFCF in Vietnam increased quickly in the first five years, reaching its highest level in 1994 (about 50 per cent). However, after that, the share of FDI in GFCF decreased because of the slow down in new FDI and the expansion of public and domestic private investment. By 2005, the FDI share in fixed capital formation was about 15 per cent. Compared with the other four countries (Singapore, China, Malaysia and Thailand), the role of foreign investment in Vietnam was relatively higher, standing second behind Singapore. The third indicator FDI/GDP ratio, has the same trend, i.e., reaching a peak in 1994 (11.9 per cent) and then going down to nearly 4 per cent of GDP in 2003. However, this ratio in Vietnam is still higher than in China and Malaysia even though the value of capital flow is much lower.

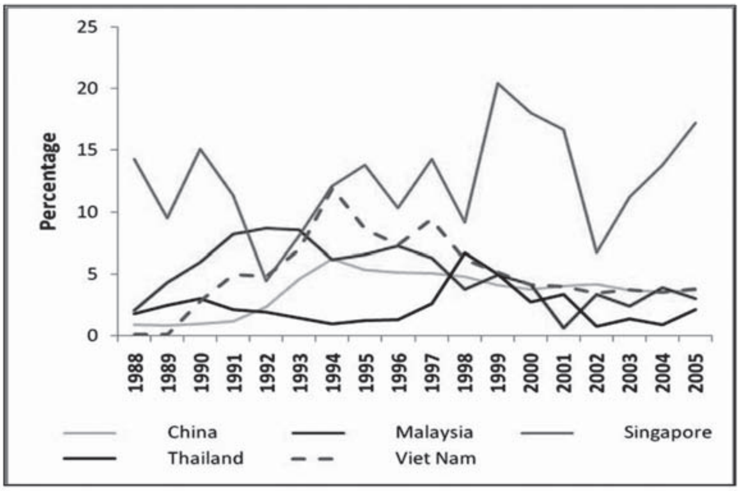
The ownership shares in gross domestic investment (Table 3) give further indication of the contributions from the three ownership types

FIGURE 2
FDI Inflows as Percentage of Gross Fixed Capital Formation (GFCF)



SOURCE: UNCTAD FDI database online, 2006.

FIGURE 3
Inward FDI Flows as Percentage of Gross Domestic Product (GDP)



SOURCE: UNCTAD FDI database online, 2006.

TABLE 3
Composition and Growth of Total Investment for Development
(In percentages)

Year	Composition (%)			Growth index: 1994=100			
	FDI	Domestic private	State-owned	FDI	Domestic private	State-owned	Total
1985	0.0	28.5	71.5	0.0	25.3	52.0	27.8
1986	0.0	40.2	59.8	0.0	34.0	41.2	26.4
1987	0.0	47.2	52.8	0.0	38.0	34.8	25.3
1988	2.5	44.2	53.3	2.4	40.4	39.9	28.6
1989	13.6	40.9	45.5	14.4	42.1	38.4	32.3
1990	13.1	46.7	40.2	17.5	61.0	42.9	40.8
1991	14.3	47.7	38.0	22.8	73.8	48.0	48.4
1992	21.0	43.9	35.1	51.1	103.8	67.9	74.0
1993	25.2	30.8	44.0	83.7	99.4	116.0	101.0
1994	30.4	31.3	38.3	100.0	100.0	100.0	100.0
1995	30.4	27.6	42.0	119.0	105.0	130.7	119.1
1996	26.0	24.9	49.1	117.0	109.0	175.4	136.9
1997	28.0	22.6	49.4	150.1	117.8	210.6	163.2
1998	20.7	23.7	55.5	114.4	127.0	242.8	167.5
1999	17.3	24.0	58.7	104.6	141.2	281.7	183.9
2000	18.0	22.9	59.1	125.4	154.9	327.3	212.0
2001	17.6	22.6	59.8	138.1	172.0	372.3	238.4
2002	17.5	26.2	56.4	156.6	228.0	401.4	272.7
2003	16.3	29.7	54.0	165.4	291.7	434.4	308.0
2004	15.5	30.9	53.6	175.1	338.8	481.2	343.6
2005	15.7	32.1	52.2	204.7	397.8	527.4	388.3
2006	16.2	38.1	45.7	249.7	461.4	579.6	441.5
2007[a]	24.8	35.3	39.9	482.5	541.7	621.9	555.4

NOTE: a. Preliminary estimate from GSO website, 2007.
SOURCE: CEIC Asia Database, 2006.

(foreign-owned, domestic private and state-owned) to total investment for development in Vietnam since 1985. Using this indicator, the trend of FDI share in total investment is almost similar. In the first reform period, domestic investment was relatively small and increased slowly as the old economy mechanism was slowly reformed. The foreign share in total investment in this period increased from 0 per cent in 1985 to 30.4 per cent in 1994. From 1996 onwards, foreign investment fell relative to domestic investment. On average in the second period, FDI accounted for 20 per cent of total investment. On the other hand, the share of domestic private investment declined sharply in the first period (1985–94) and then reduced slowly until 2002. This is explained by the structural change in the economy as a result of *Doi Moi*. In the past, collectives had played an important role in the economy, especially in rural areas. The reform toward a market-oriented economy forced most agricultural collectives to close down or transform into service provider in corporate sector.

With the recent policy improvement, especially the new Law on Enterprises and the Investment Law, both FDI and domestic private sectors have developed quickly, contributing to 24.8 per cent and 35.3 per cent of total investment for development, respectively.

Although the proportion of public investment decreased significantly from about 60 per cent in 2001 to 40 per cent in 2007, this sector still dominates with a stable share in total investment of about 50 per cent during the period 1995–2008. This type of investment also achieved the highest growth index[3] by 2007 (621.9), followed by the domestic private (541.7) and the lowest growth is foreign-owned sector (482.5). Roughly speaking, a significant proportion of the public investment was for SOEs in order to guarantee the leading role of SOEs in the economy. This preference policy could become a major constraint for creating an adequate investment climate and developing the private sector.

III. Entry Mode of FDI

The stock value of FDI decomposed by form of investment in Table 4 shows 100 per cent foreign-owned enterprises dominating with 77.6 per cent of total projects and 61.6 per cent of total registered capital. Joint ventures stand second in terms of amount of either registered capital or realized capital. The figures also imply fully-owned FIEs are smaller in size than average in terms of capital, although they use more workers than any other firm types. In joint ventures, foreign investors may also provide tacit technology, management skills and know-how. Vietnamese counterparts may contribute legal knowledge, trademarks, and infrastructure in terms of mostly land and space. On average, joint ventures are much larger than fully-owned FIEs in capital stock because most of the former have been established through cooperation between foreign investors and large SOEs. Other entry modes, like BCC (Business Cooperation Contract) and BOT (Build-Operate-Transfer), are concentrated in some highly protected industries (mining and petroleum industries). Recently, a new form of investment — shareholding companies[4] has been set up and increased quickly as a consequence of the policy change that allows foreign investors to buy equity shares from domestic enterprises or to work in financial services.

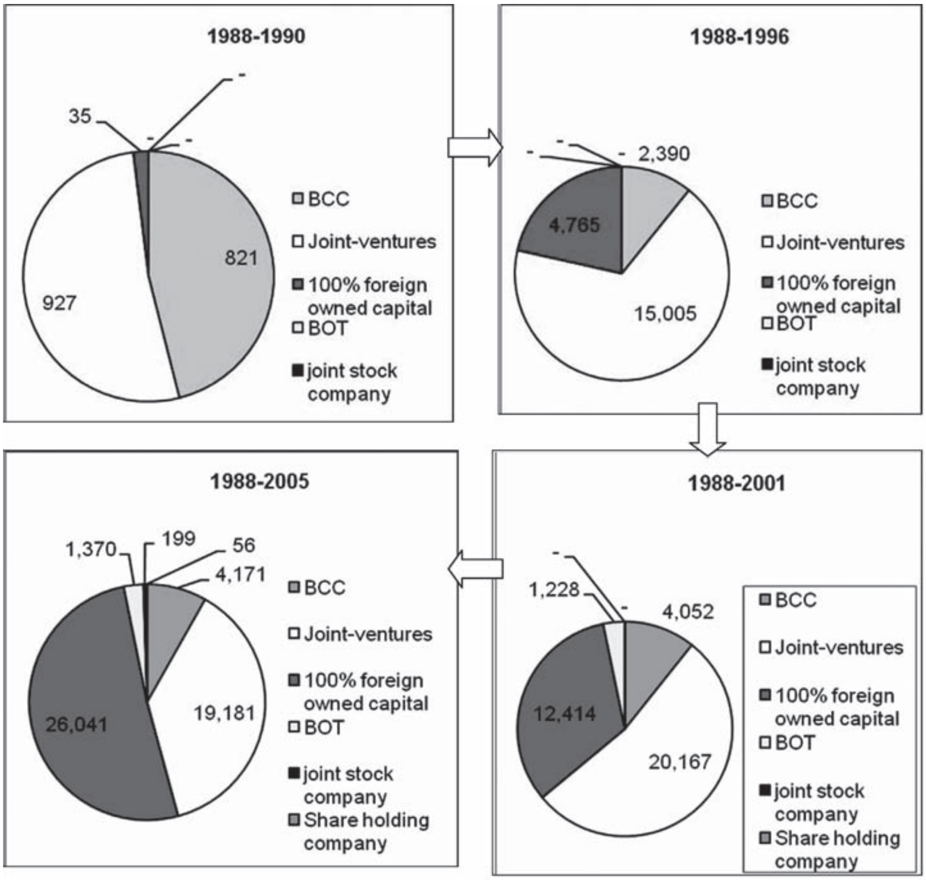
Looking at the structure of registered capital stock at different points of time in Figure 4, a remarkable adjustment amongst investment forms can be seen. In the early stages (1988–90), there were only three forms of investment and most

TABLE 4
FDI by Form of Investment as of December 2007
(Stock value, US$ million)

Form of investment	*No. of Projects*	*Registered capital*	*Realized capital*	*% of projects*	*% of Registered capital*	*Realized/ Registered capital*
Fully-owned FIEs	6,743	52,437	11,324	77.6	61.6	21.6
Joint-ventures	1,640	24,575	11,145	18.9	28.9	45.4
BCC	226	4,579	5,661	2.6	5.4	123.6
BOT, BT, BTO	8	1,711	727	0.1	2.0	42.5
Shareholding company	67	1,756	377	0.8	2.1	21.5
Total	**8,684**	**85,057**	**29,234**	**100.0**	**100.0**	**34.4**

SOURCE: Database of MPI on website, 2008.

FIGURE 4
Change in Form of Investment over Time
(Registered FDI, US$ million)



SOURCE: MPI database (various sources).

foreign investors preferred to cooperate with SOEs (joint ventures) to access government preferential treatment on credit, land ownership and other administrative procedures. The engagement of foreign investment in joint ventures may also reflect the high risk and uncertainty in the economic environment at that time. Moreover, foreign investors had to rely on cooperation with SOEs because development of the domestic private sector was not equally encouraged at that time. In the second period (1991–95), those three forms of investment became more equal with a significant increase in fully-owned FIEs. Nevertheless, joint ventures continued to increase because foreign investors were only allowed to establish joint ventures in many protected industries. Joint ventures were still a driving force with more than two-thirds of total registered capital. Since 2001, evidence reveals a decrease in the share of joint ventures in total registered capital as well as the share in a number of projects. The last episode (2001–2005) observed two fundamental changes. One is that the forms of investment were more diversified with the participation of two more entry modes (shareholding companies and capital holding companies). Another was that fully-owned FIEs overwhelming joint ventures and other entry modes. There were two main reasons for this. Policy reform had significantly improved the investment climate and foreign investors were now allowed to set up any form of investment in most industries and services. They seemed to follow the trend in preferring to form fully-owned enterprises, probably in order to avoid benefit conflict and make business decisions easily. Second, there was a huge increase in the number of domestic firms although most were at low competitive capacity. Therefore, cooperating with domestic firms in terms of forming a joint venture is not the best solution. MNEs with their comparative advantages easily compete in taking market power.

Entry mode diversification has become popular in most FDI host countries as there has been a rapid increase in FDI in the form of M&A compared to Greenfield investment (UNCTAD 2006). In the case of Vietnam, with a less developed financial market and high protection, especially for SOEs, most ownership transformation has occurred with direct investors preferring to set up their own corporations instead of joining with domestic partners. M&A activity in terms of forming shareholding companies was still preliminary over the past two decades, but recently, there were increasing flows of foreign capital into the stock market. See Table 4.

IV. Source-country Composition

As at December 2007, there were 9,589 FDI projects in operation in Vietnam with total registered and realized capital of over US$97 billion and US$46 billion, respectively. In terms of the source-country composition, FDI came from varied countries. In 2007, eighty-two countries and territories invested in Vietnam compared to sixty-nine in 2004. Based on the stock value of effective projects,[5] Table 5 presents information for the top ten source-FDI countries which is

TABLE 5
Top Ten Source Countries of FDI
(Stock Value as of December 2007)

Countries/territories	*Number of projects*	*Registered Capital (US$ million)*	*Realized capital (US$ million)*	*Realized/ registered*	*% of total registered*	*% of total projects*
Korea	1,857	14,398	2,738	19.0	8.9	17.3
Singapore	549	11,059	3,858	34.9	6.8	5.1
Taiwan	1,801	10,763	3,079	28.6	6.7	16.7
Japan	934	9,180	4,987	54.3	5.7	8.7
British Virgin Islands	342	7,795	1,376	17.6	4.8	3.2
Hong Kong	457	5,933	2,161	36.4	3.7	4.2
Malaysia	245	2,823	1,083	38.4	1.7	2.3
The U.S	376	2,789	746	26.8	1.7	3.5
Netherland	86	2,599	2,031	78.2	1.6	0.8
France	196	2,376	1,085	45.7	1.5	1.8
Subtotal of ten leading countries	**6,843**	**69,715**	**23,145**	**33.2**	**71.3**	**71.4**
Total country FDI	**9,589**	**97,764**	**46,594**	**47.7**	**100.0**	**100.0**

SOURCE: FDI database on website of MPI.

comprised of six Asian, three European nations and the United States. The data also show high concentration in country source of investment as ten leading countries contributed to over 70 per cent of total registered capital as well as the number of projects. Individually, Korea has surpassed Taiwan and Singapore to become the leading investment country to Vietnam. However, Japan was the largest contributor in terms of realized capital, followed by Singapore. In terms of investment performance measured by the ratio between realized and registered capital, the Netherlands stood first followed by Japan. Except for these two countries, all other leading countries have lower ratio of realized over registered capital compared to the average ratio (47.7 per cent). For instance, although Korea was the largest investor in Vietnam, its performance level was the lowest among the ten leading investors.

Table 6 shows changes in source country composition, disaggregated by conventional classification of countries and selected individuals. In general, FDI in Vietnam looked like it was following the common trend that "developed-country MNEs are less likely to invest in poorer economies with small markets, whereas developing-country MNEs tend to invest in neighbouring developing countries" (UNCTAD 2006, p. 185). For instance, FDI from developing Asian countries dominated with a share of 56.4 per cent in total investment, followed by the OECD group (32.2 per cent) and tax-haven British Virgin Islands (7.6 per cent). FDI from transition economies (excluding China) was very small, accounting for only about 1 per cent. To be more specific, registered FDI declined significantly from US$20.4 billion to US$14.7 billion between the two periods, 1996–2000 and 2001–2005.

The share of OECD capital increased from 26.4 per cent in 1996–2000 to 35 per cent in 2001–2005. This may be a positive impact as the literature argues for more advanced technology transferred from developed-world FDI than from the developing-world one. The relative increase of OECD capital in the second period was constituted by new investment from the United States, the Netherlands and Canada, and because of the sharp investment reduction from developing Asia in the second period (2001–2005). Within this group, investment from Taiwan and South Korea has substantially increased. In contrast, the drop of Singapore's FDI in the period caused a fundamental change in source-country composition and put Singapore behind Taiwan in terms of total investment in Vietnam. Mainland China also significantly increased investment in Vietnam between two sub-periods when its share rose from 0.5 to 3.3 per cent. The combination of Hong

TABLE 6
Registered FDI by Source Country (US$ million)

Country group	*1996–2000*		*2001–2005*		*1988–2005*	
	Total investment	*%*	*Total investment*	*%*	*Total investment*	*%*
OECD Countries	5,391.4	26.4	5,155.6	35.0	16,443.8	32.2
Transition/Centrally planned economies	1,426.4	7.0	96.1	0.7	571.2	1.1
Developing Asia	11,606.6	56.8	7,572.5	51.4	28,755.1	56.4
Tax-haven Islands	1,118.1	5.5	1,066.2	7.2	3,895.9	7.6
Other countries	887.2	4.3	855.8	5.8	1,352.0	2.7
Total	**20,429.7**	**100.0**	**14,746.2**	**100.0**	**51,017.9**	**100.0**

SOURCE: CEIC Asian database (for sub-periods) and MPI website for the whole period 1988–2005.
The data of MPI covers only effective projects.

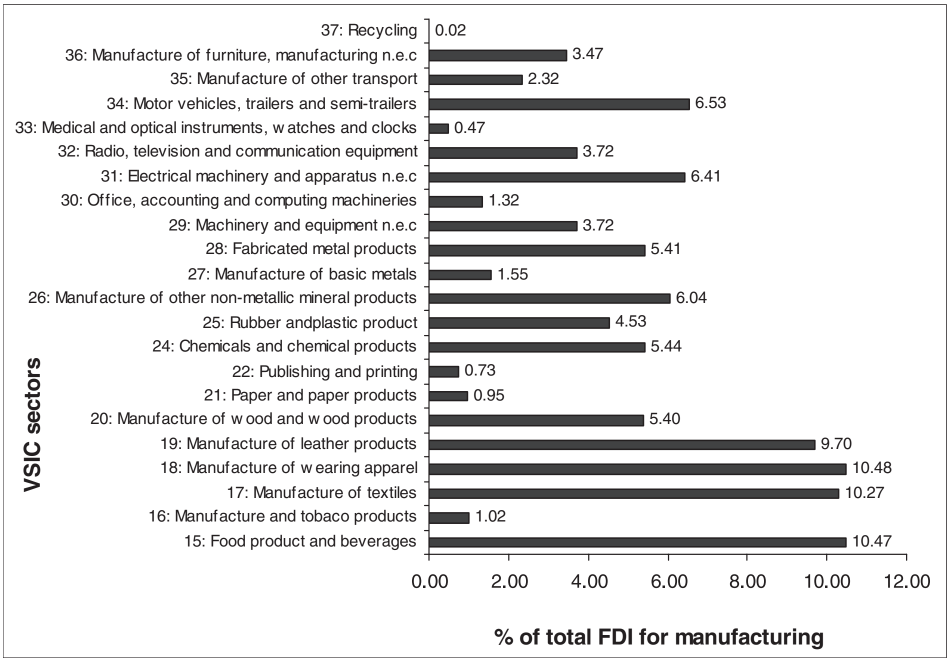
Kong and mainland China makes this country grouping one of the five largest investors in Vietnam.

Noteworthy is the FDI from two leading economies: Japan and the United States. Some studies argue that FDI from Japan and the United States has been invested indirectly through other small foreign companies in developing countries (MPI 2005). A study by MPI in 2005 compiled U.S. FDI and defines all capital invested by U.S.-based companies and their overseas subsidiaries as an indicator, "U.S.-related" FDI. The FDI undertaken by U.S.-based companies is called "U.S.-reported" FDI. The share of the capital invested through U.S. overseas subsidiaries in total U.S.-related FDI was high, from 50.0 to 80.7 per cent. In terms of capital stock, investment from U.S. overseas subsidiaries accounted for over 50 per cent of registered and 72.3 per cent of realized capital. Using U.S.-reported FDI as an indicator for country-source comparison places the United States among the top ten countries which have invested in Vietnam. Figure 5 gives more evidence on the resident country of FDI from U.S. overseas subsidiaries. Over US$800 million of U.S. capital was invested through subsidiaries in Singapore, followed by Mauritius, Bermuda, the Netherlands and Hong Kong. This study also pointed out that most of this intermediate investment was for heavy industry, foodstuff, oil and gas and was concentrated in the south of Vietnam.

V. FDI by Investment Area

To examine the effect of the new laws (Investment Law and Law on Enterprises) on FDI inflows, Table 7 shows data on accumulative FDI in the

FIGURE 5
Compositions of FDI Flows to Manufacturing Industry in 2000–2002
(Approval and Total Project Cost Basis)



SOURCE: ASEAN Secretariat, ASEAN FDI database, 2003.

TABLE 7
Sectoral Compositions of FDI Stock in 1988–2008
(For Effective Projects Only)

Sector	*Number of Projects (2008)*	*Registered capital in 1988–2005*		*Registered capital in 2006–2008*		*Realized capital in 1988–2007*	
		Value (US$ million)	*Composition (%)*	*Value (US$ million)*	*Composition (%)*	*Value (US$ million)*	*Composition (%)*
Primary production	**886**	**5,357**	**10.5**	**13,444**	**13.6**	**7,001**	**23.9**
Crude oil	48	1,891	3.7	12,587	12.7	5,148	17.6
Agriculture and forestry	838	3,466	6.8	857	0.9	1,853	6.3
Manufacturing	**5,830**	**25,447**	**49.9**	**42,067**	**42.6**	**12,916**	**44.2**
Light industry	2,740	8,471	16.6	7,209	7.3	3,639	12.4
Heavy industry	2,602	13,528	26.5	33,637	34.1	7,050	24.1
Foodstuff	350	3,139	6.2	1,060	1.1	2,058	7.0
Seafood	138	309	0.6	161	0.2	169	0.6
Construction	**802**	**11,526**	**22.6**	**24,119**	**24.4**	**4,729**	**16.2**
New resident Park	563	4,011	7.9	2,267	2.3	2,150	7.4
New cities	14	2,552	5.0	5,673	5.7	111	0.4
Office-building	189	3,937	7.7	15,425	15.6	1,892	6.5
EPZ&IZ, infrastructure construction	36	1,026	2.0	755	0.8	576	2.0
Service	**847**	**8,688**	**17.0**	**19,127**	**19.4**	**4,588**	**15.7**
Transportation & tele-communication	235	2,924	5.7	3,331	3.4	722	2.5
Hotel, Tourism	250	2,864	5.6	12,548	12.7	2,401	8.2
Finance-Banking	68	788	1.5	270	0.3	715	2.4
Cultural-Health-Education	294	908	1.8	851	0.9	367	1.3
Other services	1,438	1,203	2.4	2,130	2.2	383	1.3
Total	**9,803**	**51,018**	**100.0**	**98,757**	**100.0**	**29,234**	**100.0**

SOURCE: FDI database on website of MPI, 2006.

period 1988–2005 and 2006–2008, disaggregated by the main economic sectors. As of December 2005, half of the registered capital was allocated to the manufacturing industry. If we define infrastructure in a broad terminology as compilation of investment in construction (new resident park, new suburb, office building, and EPZ/IZ building) and investment in transportation, communication and hotel building, about 34 per cent of total registered FDI of the period 1988–2005 were invested in infrastructure development. In the past three years (2006–2008) the composition of infrastructure investment accounted for over 40 per cent. The big increase in FDI for infrastructure occurred in the 2007 and 2008 as this field lured five out of ten biggest FDI projects: New City project in Phu Yen province (US$4.3 billion), Ho Tram project in Ba Ria Vung Tau (US$4.2 billion), Gtel Mobile (US$1.8 billion), Starbay resort (US$1.6 billion) and Good Choice resort (US$1.3 billion). Before 2005, FDI was distributed equally among specific aspects of infrastructure development. Recently, most of infrastructure FDI was for building new offices (15.6 per cent) and hotel/resorts (12.7 per cent). In terms of FDI disbursement, in the whole period 1988–2007 the investment for infrastructure development was smaller than the commitment, accounting for about 25 per cent of the total realized FDI. Manufacturing industry received the biggest proportion of realized FDI in the same period (44.2 per cent). The primary sector had the best performance as the composition of realized FDI was higher than the composition of registered FDI. This is partly explained by the government policy to take advantage of the booming oil price in the period 2006–2007.

Next, the ASEAN database is used to analyse the FDI distribution within manufacturing industries. Figure 5 presents the FDI composition of every two-digit VSIC industry using total registered capital for the three years 2000–2002. It shows that FDI appears in every industry and the largest shares of this capital are in labour-intensive and export-oriented industries, such as the manufacture of leather, wearing apparel, textiles and food processing. In addition, electronics and automobile industries have also attracted a significant fraction of FDI to meet an increasing domestic demand for cars and high technology products. Although the data are only available for a short period, it can be concluded that FDI in Vietnam mostly aims to take advantage of the lower wage costs, agricultural products and the plentiful skilled and unskilled labour supply. This investment has caused a significant movement of allocation from import substitution to export-oriented industries. Based on the same source of data, Figure 6 shows that on average for 2000–2003 about 60 per cent of FDI is concentrated in export-oriented sectors.

VI. Regional Allocation of FDI

Table 8 presents the accumulative FDI (1988–2005) for six regions and ten leading provinces. Despite the Vietnamese government's effort to encourage regional diversity of FDI location, the evidence indicates a notable imbalance in FDI distribution among provinces and regions. As of December 2005, about two-thirds of FDI projects associated with over 60 per cent of total registered FDI were invested in the southeast area of Vietnam. The Red River delta was second with nearly 30 per cent of total registered FDI; these two regions accounted for about 90 per cent of total FDI. Moreover, all ten leading provinces were located in these two regions that received 84.3 per cent of total foreign investment. In contrast, fifty-four other provinces and cities received only 15 per cent of total FDI. This implies the concentration level of FDI still very much depends on conventional factors like geographical conditions (transportation costs), population density (market size), labour supply and the competition level. These areas are also more welcoming than other regions in terms of the investment climate where infrastructure development and policy openness play a decisive role.

Looking at the top ten provinces, Ho Chi Minh City was the largest recipient with 31 per cent of FDI projects and 24 per cent of registered capital, followed by Hanoi and Dong Nai. Dong Nai and Binh Duong have emerged as the most attractive

FIGURE 6
Compositions of FDI Flows to Manufacturing Industry in 2000–2003
(Approval and Total Project Cost Basis)

NOTES: Data for 2003 include FDI in the first six months only.
Export-oriented sectors including VSIC15, 17-20, 30-32 and 36 selected by the actual export/output ratio.
Y-axis: Total FDI invested in manufacturing industries in the relative term (100 per cent).
SOURCE: ASEAN Secretariat, ASEAN FDI database, 2003.

places for FDI. Although there is a clear gap in the absolute value of FDI, the gap measured by the realized/registered FDI ratio is not so large across leading provinces. FDI in the oil and gas industry is separated from provincial FDI to avoid possible distortions.

The realized FDI flows divided into four periods in Table 9 may help explain more about the geographical allocation of foreign capital. In the first period (1988–90), only five of six regions received FDI and there was extremely high concentration in the southeast area (72.4 per cent of total). In the following two periods (1991–95 and 1996–2000), FDI seemed more evenly distributed in all six regions with significant increases for the Red River Delta and the Central Coast. The last period (2001–2005, from a different and comparable data source, CEIC Asian database) was associated with a small increase in FDI for the north mountainous area, while the dominating role remained for the southeast. Across these four periods, it is easy to see better performances in the last two periods compared with the first two. However, this classification may fail to reveal the impact of the Asian crisis on FDI inflows, i.e., for the third period, the poor performance in the late 1990s (1998–2000) may be offset by the better performance in the two previous years, 1996 and 1997.

VII. Conclusion

This paper has scrutinized the trends and patterns of FDI in Vietnam since the reform was initiated in 1986. FDI inflows have fluctuated over this period, with a huge increase in the mid-1990s followed by a long-lasting depression. Recent fast changes in policy and in the investment

TABLE 8
Regional Distribution of FDI in Vietnam as of December 2005
(In US$ million)

Regions	*Number of projects*	*Registered capital*	*Realized investment*	*% of projects*	*% of Registered capital*	*Realized/ Registered capital*
Northern Mountains	158	771	307	2.6	1.5	39.8
Red River Delta	1,287	14,515	6,258	21.3	28.5	43.1
Central Coast	320	2,730	1,323	5.3	5.4	48.4
Central Highlands	88	267	178	1.5	0.5	66.7
South East	3,974	31,203	18,794	65.9	61.2	60.2
Mekong Delta	203	1,531	1,127	3.4	3.0	73.6
Total	**6,030**	**51,018**	**27,986**	**100.0**	**100.0**	**54.9**
Top ten provinces						
Ho Chi Minh	1,869	12,240	6,056	31.0	24.0	49.5
Hanoi	654	9,320	3,402	10.8	18.3	36.5
Dong Nai	700	8,495	3,842	11.6	16.7	45.2
Binh Duong	1,083	5,032	1,862	18.0	9.9	37.0
Baria Vungtau	120	2,896	1,254	2.0	5.7	43.3
Hai Phong	185	2,035	1,228	3.1	4.0	60.4
Vinh Phuc	95	774	414	1.6	1.5	53.5
Long An	102	766	332	1.7	1.5	43.3
Hai Duong	77	720	375	1.3	1.4	52.1
Thanh Hoa	17	713	410	0.3	1.4	57.5
Sub 10 provinces	**4,902**	**42,990**	**19,176**	**81.3**	**84.3**	**44.6**

NOTE: Accumulative stock of effective projects only.
SOURCE: FDI database on website of MPI.

environment under AFTA and WTO commitments have resulted in a new wave of FDI and achieving a new record in 2008 with over US$64 billion. However, there was big gap between registered and realized capital in the past three years as a result of deep decentralization without control and orientation from the central government. This is also a consequence of ongoing weakness in infrastructure, policy and human resource.

In general, the patterns of FDI shows most capital have been invested in labour-intensive or low technology industries. Before 2006, most FDI has been disbursed in manufacturing industry. However, since new Laws on Investment and Corporation became effective in July 2006, especially the accession to WTO in late 2006, the pattern of FDI has been changed as infrastructure development received an increased number of projects and registered capital. Primary production, in particular crude oil exploration also received a special attention from foreign investors as 24 per cent of total FDI disbursed but only 10 per cent of total FDI registered.

The source-country analysis revealed that most FDI originated from Asian countries with high export orientation. Vietnam has a growing FDI from the OECD, indicating the extent of advanced technology imports. The evidence also confirms

TABLE 9
Realized FDI Flows to Vietnam by Regions
(In US$ million)

Regions/episode	*1988–1990*	*1991–1995*	*1996–2000*	*2001–2005*	*1988–2005*
North mountainous area	—	109	87	421	617
Red River Delta	18	1,853	3,185	2,953	8,009
Central Coast	1	289	1,159	623	2,073
Central Highlands	0	59	73	36	167
South East	58	2,604	6,295	6,541	15,498
Mekong Delta	3	195	625	352	1,176
Total	**81**	**5,109**	**11,424**	**10,926**	**27,539**
Compositions (% of total)					
North Mountainous area	—	2.1	0.8	3.9	2.2
Red River Delta	22.3	36.3	27.9	27.0	29.1
Central Coast	1.3	5.7	10.1	5.7	7.5
Central Highlands	0.2	1.2	0.6	0.3	0.6
Southeast	72.4	51.0	55.1	59.9	56.3
Mekong Delta	3.8	3.8	5.5	3.2	4.3
Total	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

NOTE: MPI data may exclude a significant proportion of FDI managed by central level.
SOURCE: FDI database of MPI (1988-2000) and C.E.I.C Asian database (2001–2005).

FDI from the United States was indirectly invested through intermediate Asian MNEs.

In the regional distribution of FDI, the high concentration of investment is generally in two areas: the southeast and Red River Delta areas. Nine of the ten leading provinces are within these two regions, accounting for nearly 90 per cent of total investment. FDI also plays an important role in industrial zones and export processing zones (IZs/EPZs) with about one-third of total FDI invested in these areas. Foreign companies located in IZs/EPZs can take advantage of better infrastructure, incentives and support from local authorities. Deregulation for local authorities and the management boards of IZs/EPZs have created cut-throat competition among provinces in enticing FDI. However, the rapid expansion of similar IZs as a result of excessive competition in some nearby provinces has reduced the effectiveness of the policy on FDI and IZs.

Another pattern is the remarkable change in the form of investment from joint ventures to fully-owned FIEs. Initially, joint ventures were mainly established between foreign investors and SOEs and this firm type dominated in the early stage of reform (in the early 1990s). Positive changes in the investment climate (including policy reform) are the main reasons for the change in attitude of foreign investors. However, FDI in the form of M&A was still trivial compared to Greenfield investment. Implicitly, the restriction in ownership has deterred Vietnam from exploiting a highly effective finance resource for the enhancement of domestic-firm capacity and economic development.

The foreign-invested sector has played an important role in the economy of Vietnam as it contributes significantly to national investment for development, export, employment generation, GDP and state budget. Based on current situation, in future, the world economy is expected to shrink with fall in global FDI volume. MNEs have to adjust their business strategy to deal with the current global financial crisis and aftermath. Consequently, there will be a number of approved projects that may not be implemented and hence, the ratio of realized over registered capital could be further reduced. Moreover, new investors have to more carefully consider plans to set new affiliates in the host countries. If the FIE is established by bank loans, this investment would be examined and supervised more strictly. The crisis also causes decreasing demand for all kinds of goods and services. In brief, both capital disbursement and new capital inflows will be reduced significantly in the short term if the government does not pursue further improvement in investment climate.

NOTES

1. The terminology used in this paper is consistent with the Vietnamese regulations. Registered capital is total investment reported to the authority and stated in the firm's charter. Legal capital refers to the minimum capital required to establish a new firm and is also stated in the firm's charter. Realized capital (in some papers, called implemented capital) includes all assets and money invested in Vietnam.
2. Using unpublished data provided by MPI, FDI inflows to Vietnam in 2005 and 2006 surpassed the levels of Thailand and Malaysia.
3. Growth index is a ratio between the annual investment and the 1994's investment when both are measured at the 1994 constant price. It allows to compare the growth rate of the investment amongst different ownerships at a given point of time.
4. A shareholding company defined in the new Enterprise Law is an enterprise in which (a) the charter capital shall be divided into equal portions called shares; (b) shareholders shall be liable for the debts and other property obligations of the enterprise within the amount of capital contributed to the enterprise; (c) the minimum number of shareholders shall be three and there shall be no restriction on the maximum number; and (d) shareholders may freely assign their shares to other persons.
5. Effective projects refer to projects implemented at the point of time. Therefore, failed and outdated projects are excluded from the FDI data.

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