Chapter 5

Foreign Direct Investment and the Industrialisation of Viet Nam

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1. Introduction

This chapter considers the history of foreign direct investment (FDI)¹ in Viet Nam and how FDI has influenced the industrialisation of Viet Nam.

Johnson (1972) said that the essence of FDI is the ‘transmission to the ‘host’ country of a ‘package’ of capital, managerial skill, and technical knowledge’. These benefits are not limited to developing countries but will be affected in various ways by high-productivity FDI, even in developed countries. Kimura and Kiyota (2007) showed the high productivity levels and growth of FDI firms in Japan in the late 1990s and pointed out the direct effect of FDI on host countries in beneficial assets, such as technology, management capabilities, and corporate governance.

In this way, it has been noted that FDI has a beneficial effect on host countries. Since the 1980s, Southeast Asian countries have focused on attracting FDI, including Japanese companies, because FDI complements the scarce capital and technology of developing countries (Blomstrom and Kokko, 1998). Since the early 1990s, when Viet Nam began to work on full-fledged reform and opening-up policies, it has been working to attract FDI in order to achieve stable and sustainable economic growth.

The acceptance of FDI has allowed Viet Nam to achieve direct effects, such as job creation and export expansion. In addition, the opening of the home market to high-productivity FDI also had an indirect effect on the modification of old economic structures, such as state-owned enterprise reform. The opening of the home market to FDI has required old-type companies that have been guaranteed activities through subsidies and monopolies to make further management efforts, such as improving management efficiency and diversification and developing new markets by expanding overseas. This is a change that can be an advantage for reform promotion, whilst it is a disadvantage for the defending old faction that the efficiency improvement of the home country’s economy is promoted by accepting FDI.

Again, when developing economies accept FDI from developed countries, host countries can accept capital and high-technological capabilities. If this direct effect is the first effect, the second effect is the indirect effects, also known as spillover effects, such as the transfer of know-how to local companies and encouraging the productivity improvement of other companies in the industry through competition (MacDougall, 1960). As a third effect, FDI has the effect of promoting structural reforms, such as the deregulation of the host country (Blomstrom and Kokko, 1998), which is expected to bring the economic system closer to international standards.

¹ Unless otherwise noted in this chapter, FDI refers to inward direct investment from abroad to Viet Nam.
In this chapter, Section 2 presents an analytical viewpoint for observing the intra- and inter-industrial spillover effects of FDI on the Vietnamese economy. Section 3 explains that Viet Nam’s FDI initially started with an import substitution industry and then moved to export-oriented FDI after Viet Nam joined the World Trade Organization (WTO). Furthermore, the section outlines the characteristics of FDI by country, region, and industry, and outlines the existence of the direct impact of FDI through the composition ratio of FDI in major economic indicators. In Section 4, we discuss intra-industrial spillovers using the capital equipment ratio and discuss whether or not there is a backward linkage effect on inter-industrial spillovers from the trade data by the production process. Section 5 focuses on the role of FDI in the industrialisation of Viet Nam as a conclusion, and discusses the steps needed for future industrialisation.

2. Analytical Perspective

2.1. Impact on FDI Host Countries

Figure 5.1 is a conceptual diagram by Iwasaki (2013), it shows how FDI affects a host country. The effect on the host country is divided into direct and indirect effects. The direct effect is that it increases the productivity ratio in the capital of the host country through the investment of the highly productive FDI, so macro productivity also increases if there is a ‘composition effect’. If FDI enters the host country through a joint venture with a local company, it will also bring ‘improvement effects’ in the traditional management of the local company through the participation of FDI as a partner.

On the other hand, the indirect effect is that the addition of highly productive FDI to a specific industry has a positive impact on surrounding industries through the market. This effect is called the spillover effect, and it can be divided into the spillover effect within the horizontal intra-industry and the spillover effect between vertical inter-industries. Horizontally, the incentive to improve productivity works for other companies in the same industry in the host country, and consequently leads to productivity improvement in the entire industry. However, according to Caves (1974), analysis of the spillover effect of FDI from developed countries to Canada and Australia in the 1960s shows that FDI in developed countries ended up dominating the market. The reason for this is that companies in developing countries have poor technological capabilities and there is a big difference in competitiveness compared to developed countries. Further, a case study of Venezuela by Aitken and Harrison (1999) also confirmed the negative effects.

On the other hand, vertical inter-industrial spillovers are due to the high-efficiency production activities of FDI companies spreading between industries through forward and backward linkage effects. In the manufacturing industry, the forward linkage is that if the production ratio of highly efficient FDI increases in the production process in the middle stream of the industry, the productivity of the production process in the downstream industry will also increase. Conversely, the backward linkage is a spillover effect from the middle stream to the upstream process. Previous research has shown positive and significant results of this vertical spillover effect in analysis of Lithuania by Javorcik (2004) and Blalock and Gertler (2008) in Indonesia. Iwasaki (2013) also revealed the forward linkage effect of FDI in Japan, which increased the productivity of manufacturing companies located downstream as the foreign capital ratio in the upstream process increased.
Figure 5.1. How FDI Affects a Host Country

Effect of inward FDI

Direct effect

Composition effect

Improvement effect

Horizontal intra-Linkage effect

Indirect effect (effect on companies in host country)

Forward Linkage

Vertical intra-Linkage effect

Backward Linkage

2.2. Backward and Forward Linkage Effects

According to Hirschman (1958), ’The input-provision, derived demand, or backward linkage effect, i.e., every nonprimary economic activity, will induce attempts to supply through domestic production the inputs needed in the activity.’ Conversely, the effect of expanding demand in expanding upstream industry production, and the effect of expanding the production of downstream industries, are called the forward linkage effect. As examples of the backward linkage, if clothing production explodes, it will induce the domestic production of intermediate materials, such as fabrics and yarns, in the middle stream of industry and more; also, the expansion of smartphone production will encourage the domestic production of modules and parts.

Figure 5.2 is a conceptual diagram that shows how FDI and local companies relate to the process of industrial production. The FDI of the advanced country enters the developing country for export-oriented production because there is a comparative advantage in the labour force in the host country. In addition, since domestic demand in the developing country is so small, FDI enters as an export-oriented type. The first step of FDI is the entry of labour-intensive and export-oriented types of FDI.

The main industries of the first step will be primarily triggered by FDI companies and will focus on the assembly process of final products, such as clothing, footwear, smartphones, personal computers, and so on. This is because local companies lack capital, technology, and marketing capabilities in the global market, and it is difficult for local companies to enter the final goods production processing of smartphones and personal computers.

In the second step, the large production scale of the final goods will encourage the entry of FDI in the field of intermediate goods, processing materials, and parts and components production by the backward linkage effect. Intermediate goods production is in the middle stream of the process and is a capital-intensive industry. In general, local companies do not have large-scale capital and advanced technology and will not be the main players in intermediate goods production.

The third step is the stage where local companies get business opportunities with FDI through contracting or sub-contracting processing for intermediate goods production. Such local base industries will internalise capital, make additional capital investments, and raise their technical level. Some local companies will become the primary suppliers who do business directly with the final goods manufacturers. Currently, Samsung Electronics of the Republic of Korea (hereafter, Korea) is
exporting and producing smartphones on a large scale in northern Viet Nam, but the Samsung group’s companies responsible for module production, and its cooperative FDI companies, are also expanding investment into Viet Nam. It is said that 25 Vietnamese domestic companies are joining the supply chain as first suppliers and 190 as second suppliers (Viet Nam News, 2017). Looking at Viet Nam’s smartphone supply chain, it can be said that the current industrialisation phase in Viet Nam is in the third step.

After that, as the fourth stage in the production of final goods, local companies will produce the final goods by themselves in addition to contract production such as original equipment manufacturing (OEM) and original design manufacturing (ODM). In Viet Nam today, the local manufacturing industry has not established a world-class brand, and Viet Nam’s industrialisation has yet to reach the fourth step.

However, Vingroup, a local, private Vietnamese conglomerate that has grown rapidly due to the real estate development business, manufactures vehicles and sells them under its own brand to the global market, and can be said to be taking on the challenge of the fourth step. It has also announced plans to start exporting to the world market, invest in building its own factory in North Carolina in the United States, and start producing electric vehicles in 2024 (Nikkei Asia, 2022).

**Figure 5.2. Progress in Industrialisation and the Relationship Between FDI and Local Companies**

Source: Author.
2.3. Summary of Analytical Viewpoints

This chapter considers the effect of FDI on industrialisation in Viet Nam and the inter-industry and intra-industry spillovers. First, for intra-industry, it will examine specific industries with a high FDI ratio amongst manufacturing industries and focus on the changes in the capital equipment ratio per worker in those industries. The capital equipment ratio is the amount of fixed assets (equipment, land, buildings, etc.) divided by the number of employees in the industry. The progress of the mechanisation of individual industries can be seen. If it is at a low level, it can be said that it is labour-intensive, and if it is at a high level, it is capital-intensive. In addition, the increase in the capital equipment ratio over a certain period of time can be considered to lead to new capital investment and an improvement in productivity. On the other hand, a decline in the capital equipment ratio indicates that new business fixed investment has not progressed, and labour has been consolidated.

Marukawa (2003) conducted a study of industrialisation in Viet Nam using the capital equipment ratio. The study showed that from the capital equipment ratio, the country’s machinery-related industries were not capital-intensive in 1999. In terms of ownership, it was derived that industries with frequent entry of FDI were capital-intensive and relatively productive. In addition, Tho (2010) analysed and found that the export ratio and capital equipment ratio in 23 manufacturing sectors in 2002 were inversely correlated. In other words, it was found that the capital equipment ratio of industries that had a high export ratio, such as manufacturers of leather, furniture, wood, and clothing was low, and the capital equipment ratio of industries with a low export ratio, such as non-metallics and steel, was high.

Next, the inter-industrial spillovers will be observed from the import and export statistics of industries with high FDI ratios by the trade specialisation coefficient (TSC), and the inter-industry spillover effects will be derived from the trade structure of the final goods and parts. If the host country receiving the FDI assembles and exports labour-intensive final goods on a large scale, it will also need and receive new FDI involved in the manufacture of parts and components by the backward linkage effect. It is thought that intermediate goods exports also increase because the intermediate goods production is done on a large scale for final goods production, and these intermediate goods are used also in the final goods production in another country. If it is possible to confirm that there is an export expansion of these intermediate goods, parts and components, and processed goods that also follows the export expansion of the final goods, it is possible to think that the industrialisation advances and suggests the existence of inter-industry spillover effects.
3. Entry into the International Economy and FDI

3.1. Omnidirectional Diplomacy and the Progress of Free Trade Agreements

At the end of the 1980s, Viet Nam decided to implement the Doi Moi policy, which was a reform and opening-up policy. In October 1991, the Comprehensive Cambodian Peace Agreements (Paris Peace Agreements) were concluded, and Viet Nam began to improve its foreign relations through omnidirectional diplomacy. At the end of 1991, relations with China were normalised, and in 1995 Viet Nam established diplomatic relations with the United States (US), and joined the Association of Southeast Asian Nations (ASEAN). In 1998, Viet Nam joined the Asia-Pacific Economic Cooperation (APEC), and at the end of 2001, entered into force a bilateral trade agreement with the US and gained the most-favoured nation (MFN) treatment from the US. In 2007, Viet Nam joined the World Trade Organization (WTO) as the 150th member state, developing a global standard trade environment about 15 years after it began Doi Moi. With MFN treatment from the world’s major countries, export-oriented FDI accelerated for Viet Nam.

Viet Nam’s first free trade agreement (FTA) was the ASEAN Free Trade Agreement (AFTA) in 1995, and the first bilateral FTA was the Japan-Viet Nam Economic Partnership Agreement (JVEPA) in 2008. In addition, FTA relationships also expanded as a member of ASEAN, such as ASEAN-China, ASEAN-India, and the Regional Comprehensive Economic Partnership (RCEP), and as of September 2022, Viet Nam has entered into force 15 FTAs.² As a result, Viet Nam’s FTA coverage rate has risen to 63% for exports, 81% for imports, and 73% as a whole. The reason why the FTA coverage rate for exports is low is that it does not have an FTA with the US, which is the largest export destination for Viet Nam. Singapore has the highest FTA coverage rate in Asia at 91%, followed by Viet Nam.³ Viet Nam was late in becoming a member of the WTO amongst Asian countries, and although it has been only a short time since it obtained a world-standard trade environment, it has now become a country that provides the best trade environment as a production location for export-oriented FDI in Asia.

3.2. Changes in FDI and the Investment Environment

Viet Nam’s FDI reached US$176.9 billion at the end of 2020. Compared to major Southeast Asian countries, this level is 74% of Indonesia’s, 65% of Thailand’s, 1.6% above Malaysia, and 71% above the Philippines.⁴ Moreover, Viet Nam’s FDI balance had 51.9% of gross domestic product (GDP), roughly the same as Thailand (53.4%) and Malaysia (51.8%), which is higher than China (12.9%), Indonesia (22.1%) and the Philippines (28.1%).⁵

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³ Calculated using IMF statistics based on JETRO’s 2020 World Trade and Investment Report. The FTA coverage rate is the ratio of total trade value with countries/regions with FTAs in force as of the end of March 2022, and was calculated based on the 2019 trade statistics.
⁵ GDP is based on IMF ‘World Economic Outlook’ (accessed 27 February 2022).
In phase 1, Viet Nam started Doi Moi and opened its doors to FDI. It was a time that could be called the flowering period. The FDI of Viet Nam was very small before Doi Moi and came from the former Soviet Union and Eastern European nations. According to *Far Eastern Economic Review* (FEER, 1993a), when Viet Nam launched the Doi Moi policy and started to improve foreign relations, it attracted worldwide attention as an untouched market of more than 70 million people. However, the actual FDI expansion had to wait until the lifting of the US economic sanctions against Viet Nam in 1994 (The Economist, 1994). FDI in the mid-1990s was preceded by large-scale investment in crude oil prospecting and mining rights, and import-substitution-type investment in the manufacturing industry began on a small scale.

The main investment countries and regions in Viet Nam were from Asia, such as Japan, Korea, Singapore, and Taiwan, and in addition to resource development and import substitutitional manufacturing, there were real estate investments, such as hotels, apartments, and office buildings. The import substitution type of manufacturing investment preceded this because Viet Nam at that time was not granted MFN treatment from the US, and the export market was limited. Therefore, the FDI enterprises for durable consumer goods, such as cars, televisions, and motorcycles, came to invest under the import substitution industrialisation policy on the condition of import protection.

Figure 5.3 shows the annual flows of FDI in Viet Nam since 1990 divided into four periods based on the characteristics, such as the historical background.

Figure 5.3. Viet Nam’s FDI (Flow) Trends in Four Periods (US$ million)

Source: UNCTAD Stat.

(1) Phase 1: Import substitution (1990–1997)

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However, import substitution industrialisation policies are generally said to have a negative effect on the host country's economy, e.g., Encarnation and Wells (1986) and Wells (1993). This is because the import substitution industry is an industry without international competitiveness protected by import barriers, and in markets with small domestic demand and a lack of economies of scale, products will continue to be supplied at high prices to domestic markets. In addition, many previous studies have pointed out that FDI policy attracts more FDI by adopting an export-oriented, open trade policy rather than a protectionist policy, e.g., McCulloch (1993) and Ohno (1998).

Let us take a look at the history of import substitution industries in Viet Nam. FDI started television (TV) production in Viet Nam from China, Japan, and Korea in the 1990s. In the case of Japanese companies, there were already TV factories of affiliated companies in ASEAN countries, such as Thailand, Malaysia, and Indonesia. If ASEAN is integrated into the economy in the future, it will be essential to reorganise by optimal production, and TV production in Viet Nam has become difficult. In addition, since the 2000s, Japanese brand TVs have been pushed out by Korean and Chinese brand TVs in the global market, and many Japanese manufacturers have withdrawn from in-house production of LCD panels. Currently, TV production in Viet Nam is doing well as an export-oriented industry, such as Samsung Electronics and LG from South Korea and TCL from China.

Next, according to the Vietnam Automotive Manufacturers’ Association (VAMA), 17 companies are currently assembling and processing automotive production for the domestic market, including global manufacturers, such as Toyota, Ford, and Honda, as well as local commercial vehicle production companies. In 2021, the market size for new vehicles sold in Viet Nam was quite small, at 277,203 units.

According to FEER (1993b), in the early 1990s, the Vietnamese government said it would approve only seven manufacturers (three for commercial vehicles, two for heavy commercial vehicles such as trucks and buses, and two for passenger cars), but ultimately 14 FDI companies were approved. Although the size of the vehicle market in Viet Nam has gradually expanded, Viet Nam’s automobile production volume in 1995 was 3,500 units per year, reaching 10,000 units in 2000 and exceeding 100,000 units in 2008. Even Toyota, with the largest market share in Viet Nam, sold just under 70,000 units in 2021. Furthermore, most of them were imported from Thailand and Indonesia; there were only a few locally assembled vehicles. Because of the small market size in Viet Nam, there are few FDI companies in the parts industry, and although more than a quarter of a century has passed since the start of operations, international competitiveness cannot be acquired.

On the other hand, since the 1980s, the motorcycle industry has had a history of an influx of finished vehicles and assembly parts kits from neighbouring countries, such as Thailand and China, both officially and informally. In the 1990s, Japanese manufacturers Honda, Suzuki, and Yamaha and other manufacturers from Taiwan and Korea entered Viet Nam’s market as import substitution and domestic production began. However, unlike the automotive industry, import restrictions on motorcycles were not strictly enforced, and in 2000, a large number of assembly kits were imported from China, and the import substitution industry policy of the motorcycle industry practically did not work. On the other hand, it can be said that the imperfection of such import restrictions has consequently strengthened the competitiveness of the domestic motorcycle industry (Ikebe, 2020).

Ohno (1996) said Viet Nam should promote free trade whilst still pursuing maximum transitional measures to foster domestic industries. In other words, rather than developing local companies...
protected by import barriers until they can withstand international competitiveness, it is a strategy of attracting labour-intensive and export-oriented FDI so that local enterprises can gradually acquire industrialisation from the intra-industry and inter-industry spillovers.

Viet Nam during the import substitution period attracted attention from all over the world for its reform and opening-up policy and the improvement of foreign relations through omnidirectional diplomacy. However, the business environment was insufficient, including the FDI-related legal system, hard infrastructure, and the trade environment necessary for export-oriented FDI to enter the market. Further improvement of the conditions for accepting FDI was urgently needed.


Phase 2 was a period of implementation of domestic institutional reforms for bilateral trade agreements with the US and the WTO accession, whilst FDI was sluggish due to the recession caused by the Asian currency crisis. Viet Nam enacted as many as 500 laws, including the revision and abolition of existing legal systems, in order to join the WTO (OECD, 2018). During this period, Viet Nam implemented reforms, such as free trade and open market policy from import substitution protectionism, the reorganisation of state-owned enterprises, and the improvement of the global standard business environment for FDI.

In 2000, bilateral trade negotiations with the US, which were a prerequisite for joining the WTO, were finalised, and the US-Viet Nam Trade Agreement entered into force at the end of 2001. This gave Viet Nam MFN treatment from the US, and US import duties on Viet Nam were significantly reduced from the previous average of 40% to less than 3%. Meanwhile, Viet Nam had promised to open up the service market and protect intellectual property rights (Manyin, 2002). Although Viet Nam’s exports to the US increased significantly due to entry into force of the US-Viet Nam Trade Agreement, it did not trigger FDI inflows into Viet Nam. One factor was that Viet Nam’s exports to the US were mainly consignment processing industries, such as clothing, footwear, and processed fishery products, and it was possible to implement these in a form other than FDI.

Viet Nam’s negotiations to join the WTO faced a number of challenges, including improved market access offers in goods and services, agriculture, domestic support and export subsidies, phasing out of dual prices, progress in phasing out local content policies, efforts in complying with the intellectual property (TRIPS) agreement, and restructuring state enterprises, etc. (WTO 2003). In 2005, the Investment Law and the Enterprise Law, which aimed to meet the WTO’s national treatment, trade-related investment measures (TRIMs), and TRIPs standards came into force (The American Lawyer, 2009).
In 2003, the Ministry of Planning and Investment (MPI) of Viet Nam, the Japanese government, and the Federation of Economic Organizations co-chaired the Japan-Viet Nam Joint Initiative to evaluate requests, action plans, and progress to improve the investment environment. Until now, dialogue has been held on a wide range of investment environment improvements, including the development of supporting industries, the development of legal systems, human resource development, transportation and customs clearance, intellectual property rights protection, the improvement of living environments around industrial parks, and food safety, etc. In October 2021, Phase 8 of the joint initiative began. Implementing the joint initiative will improve the business environment and ensure the international competitiveness of FDI companies, structural reforms to promote investment for Viet Nam, and, if necessary, also lead to the possibility of official development assistance (ODA) being implemented.

In this way, Phase 2 was a period of stagnation for FDI, but at the same time, it was also a period when Viet Nam implemented policy efforts to attract FDI. As Blomstrom and Kokko (1998) point out, FDI promotes structural reforms in the country. In Viet Nam, reforms for deregulation and trade liberalisation to attract FDI were promoted.


Phase 3 was triggered by the accession to the WTO in 2007, and export-oriented FDI expanded rapidly. FDI expanded sharply in 2007 and 2008 and remained as high as US$7 billion–US$9 billion. By joining the WTO, Viet Nam was granted MFN treatment from the world’s major markets, gaining a trade environment for export-oriented FDI expansion. Due to the increase in export-oriented FDI, Viet Nam’s share of FDI in exports rose to 67.4% in 2014 from 57.7% in 2007 (General Statistics Office of Vietnam (GSOV)).

Viet Nam has since participated in negotiations new FTA, including participation in the Trans-Pacific Economic Partnership (TPP) Agreement in 2010 and the start of FTA negotiations with the European Union (EU) in 2012. From the viewpoint of economic security, the diversification of trading partners was urgently needed for Viet Nam, and it was important to acquire a higher-level and wide-ranging free trade environment to accumulate export-oriented FDI. In particular, the US and EU countries, which have not signed FTAs with Viet Nam, were large export destination markets, and further expansion can be expected if FTAs are realised. In this way, Viet Nam, which wants to promote the diversification of its trade structure, has shown its willingness to actively engage in free trade even after joining the WTO, and it has become an increasingly attractive investment destination for export-oriented FDI.

The representative FDI for Phase 3 was Samsung Electronics of Korea, which began the production and export of smartphones in northern Viet Nam in 2009. Samsung’s large-scale smartphone exports eliminated the trade deficit in 2014, the first time since the 1990s. In 2020, Viet Nam’s exports of smartphones accounted for 22.0% of the country’s exports (UN Comtrade).

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(4) Phase 4: Making a leap (2015–present)

2015, the starting point of Phase 4, was the year when Viet Nam's trade environment and liberalisation leapt ahead, with a broad agreement on the TPP negotiations in Atlanta (US), reaching the final agreement on the EVFTA, the inauguration of the ASEAN Economic Community (AEC), and the expected acceleration of RCEP negotiations. More and more export-oriented FDI accumulated in Viet Nam, becoming an FTA power.

The US then left the TPP, and a new Comprehensive and Progressive Agreement on Trans-Pacific Partnership (CPTPP) was signed by 11 countries, excluding the US. In Viet Nam, the CPTPP came into force in 2019, the EVFTA in 2020, and RCEP in 2022. These new-era mega-FTAs are expected to increase Viet Nam’s exports further (Viet Nam News, 2022).

Meanwhile, from around 2018, the US-China conflict became apparent, and the movement to transfer China’s export production to the US to Viet Nam accelerated due to trade conversion (Nikkei Asia, 2020a). According to UN Comtarde, In 2020, Viet Nam’s exports to the US increased significantly, and items such as smartphones, tablet PCs, furniture, plastic products, toys, and exercise equipment increased by 2–4 times compared to 2017. According to IMF

“Direction of Trade Statistics (DOTS), Viet Nam’s exports to the US in 2020 jumped 1.9 times from 2017, and its trade surplus with the US nearly doubled from US$32.2 billion in 2017 to US$63.4 billion in 2020. Despite Viet Nam’s diversification of its trading partners, its dependence on US exports rose from 19.5% to 27.8% over the same period, and its dependence on imports from China rose from 26.0% to 32.6%. The trade conversion effect caused the transfer of manufacturing and processing industries, including FDI, from China to Viet Nam.

3.3. FDI in Viet Nam

(1) Overview of FDI

Figure 5.4 shows the developments in FDI in terms of each year-end balance in Viet Nam. A breakdown by region shows that in 1996, at 52.8%, more than half of the total FDI was concentrated in southern Viet Nam. According to GSOV Web site and Statistical Yearbook of Hochiminh city, Ho Chi Minh City, the core city of the southern region of Viet Nam, is the largest economic city amongst the municipalities under the direct control of the central government, and in 2000, the city’s population share was 6.7% of the national population and 17.2% of GDP. The economic scale of the southern part of the city, including the surrounding provinces of Ho Chi Minh City, is larger than the northern region centred on Hanoi City, and this structure has continued to this day.
In the mid-1990s, Viet Nam’s national income was low, the service industry market was immature, and the entry restrictions on FDI were strict, making it difficult for FDI to enter the market in areas such as retail, food and beverages, finance, and transportation (logistics in the domestic market). For this reason, although manufacturing accounted for most of the FDI, infrastructure development, such as industrial parks, stable power supply, airports and seaport facilities, was necessary to attract more manufacturers. In this regard, the southern region provided a relatively better investment environment than the northern region. In addition, export-oriented FDI was not a joint venture with a local company but aimed to enter the market with 100% foreign capital. However, in Viet Nam in the 1990s, it was difficult for FDI to lease land in general areas, and only industrial parks and export processing zones could receive FDI by 100% foreign capital.

In southern Viet Nam, according to the Hochiminh city Export Processing and Industrial Zones Authority (HEPZA), the Tan Thuan Export Processing Zone, built with Taiwanese investment in 1991, and the Linh Trung Export Processing Zone, opened by Chinese investment in 1992, attracted FDI in the manufacturing sector. On the other hand, in northern Viet Nam, the delayed development of industrial parks led FDI to enter the country through joint ventures with state-owned enterprises, facilitated by leasehold financing. This particular type of FDI was characterised by import substitution industries such as automotive, motorcycle, and television manufacturing. In this way, Toyota, Honda, and Yamaha of Japan, Ford of the US, and LG Electronics of Korea entered the northern part of Viet Nam in the 1990s.

The development of the northern industrial parks included the opening of the Nomura-Haiphong Industrial Zone in the port city of Haiphong in 1994 and the Tang Long Industrial Park on the outskirts of Hanoi in 1997. However, due to the delay in developing infrastructure around industrial parks, including roads and ports in the north, and the economy’s deterioration due to the Asian financial crisis, the amount of FDI in the manufacturing sector was small and remained sluggish until the early 2000s.

In the 2000s, Canon, a major Japanese printing machinery company, entered the Tang Long Industrial Park and began the large-scale export production of inkjet printers (FEER, 2003a). Canon’s entry into the region triggered a large number of export-oriented FDI companies to enter the northern region. However, China coming to be called the world’s factory because of the concentration of export industries, the spread of the infectious disease SARS, the introduction of the renminbi management floating exchange rate system, anti-Japanese demonstrations, and the Sichuan Earthquake occurred one after another in the mid-2000s. In order to deal with the risk of overconcentration in China, a movement called ‘China Plus One’ began to be recognised amongst Japanese companies (Harney, 2008; Ikebe, 2012). This was to diversify risks by allocating production bases concentrated in China to countries other than China. An excellent opportunity to accept diversified investments from China, Viet Nam, and other Southeast Asian countries also intensified the movement to attract FDI (FEER, 2003b). Viet Nam attracted attention as a risk diversification platform. It was easy to build a supply

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chain because it is adjacent to China and the wage level was cheap. In this way, a large number of export-oriented FDIs, such as in printing machines and smartphones, entered the Red River Delta in northern Viet Nam. Figure 5.4 shows in a breakdown by region that the FDI situation until around 2010 was concentrated in the south, but currently, it has become dispersed at 27.3% in the north and 39.1% in the south due to progress in infrastructure development.

Looking at the FDI by industry in Table 5.1, the manufacturing industry, which is the largest industry, has almost doubled its share from 29.7% in 1996 to 59.2% in 2020. Next to the manufacturing industry, the real estate industry, the supply of electricity and gas, the hotel and restaurant industry, and the construction industry accounted for a large proportion of the composition. Until 2000, the share of the manufacturing sector remained at about 30% because there was little large-scale export-oriented FDI at that time. In addition, FDI in other industries was relatively large. Although detailed figures at the time were unknown, it is thought that the ratio of large-scale FDI in the non-manufacturing industry was large, such as the telecommunications network development, crude oil and natural gas development, and petroleum refining and the real estate field. In particular, Singaporean-affiliated companies have been actively investing in the real estate field (FEER, 1993c) and industrial park development and urban development by Semcorp, a government-affiliated conglomerate, have been promoted in various places all over Viet Nam, and real estate development companies such as CapitaLand, Keppel, Fraser’s and Mapletree have also actively invested in Viet Nam. Amongst Japanese companies, conglomerates led by Sumitomo Corporation are developing smart cities in Hanoi (Nikkei Asia, 2020b).

In the 2000s, the number of export-oriented manufacturing companies producing in Viet Nam and selling in the world market in fields such as printing machinery and mobile phones increased. In the 2010s, FDI in service sectors increased due to the expansion of domestic demand and the deregulation of the service market, such as hotels/food and beverages, retail/wholesale, transportation/warehousing, and banking and insurance.

The power and gas supply business, which currently ranks third in terms of balance, is mainly through build-operate-transfer (BOT), which uses the funds and technology of FDI to develop infrastructure and will be transferred to Viet Nam after a period of operation. FDI in the form of BOT plays a role in taking over part of Viet Nam’s public works.

Looking at FDI by country and region, the country with the largest outstanding balance at the end of 2020 was Korea, followed by Japan, and FDI in these two countries was mainly in the manufacturing industry. As mentioned above, Singapore, which ranks third, has a large number of investments in the real estate field, whilst Taiwan, which ranks fourth, has a large amount
of investment in the real estate field, such as hotels and office buildings, in addition to small and medium-sized manufacturing industries. Hong Kong, which ranks fifth, is a tax haven like Singapore, and FDI from around the world, including China, is often invested in Viet Nam via Hong Kong.

### Table 5.1. Overview of FDI on a Year-end Balance Base in Viet Nam (%)

<table>
<thead>
<tr>
<th>FDI by region</th>
<th>FDI by industry</th>
<th>FDI by country and region</th>
</tr>
</thead>
<tbody>
<tr>
<td>North</td>
<td>South</td>
<td>Manufacturing</td>
</tr>
<tr>
<td>1996</td>
<td>35.9</td>
<td>29.7</td>
</tr>
<tr>
<td>2000</td>
<td>33.1</td>
<td>30.4</td>
</tr>
<tr>
<td>2005</td>
<td>28.9</td>
<td>50.1</td>
</tr>
<tr>
<td>2010</td>
<td>20.4</td>
<td>48.9</td>
</tr>
<tr>
<td>2015</td>
<td>25.9</td>
<td>57.7</td>
</tr>
<tr>
<td>2020</td>
<td>27.3</td>
<td>59.2</td>
</tr>
<tr>
<td></td>
<td>Real estate</td>
<td>na</td>
</tr>
<tr>
<td></td>
<td>Supply business, electricity and gas</td>
<td>na</td>
</tr>
<tr>
<td></td>
<td>Hotel and restaurant Construction</td>
<td>13.7</td>
</tr>
<tr>
<td></td>
<td>11.1</td>
<td></td>
</tr>
<tr>
<td></td>
<td>14.5</td>
<td></td>
</tr>
<tr>
<td></td>
<td>12.5</td>
<td></td>
</tr>
<tr>
<td></td>
<td>13.1</td>
<td></td>
</tr>
<tr>
<td></td>
<td>11.8</td>
<td></td>
</tr>
<tr>
<td></td>
<td>7.8</td>
<td></td>
</tr>
<tr>
<td></td>
<td>7.8</td>
<td></td>
</tr>
<tr>
<td></td>
<td>11.8</td>
<td></td>
</tr>
<tr>
<td></td>
<td>5.9</td>
<td></td>
</tr>
<tr>
<td></td>
<td>6.0</td>
<td></td>
</tr>
<tr>
<td></td>
<td>11.8</td>
<td></td>
</tr>
<tr>
<td></td>
<td>16.0</td>
<td></td>
</tr>
<tr>
<td></td>
<td>11.1</td>
<td></td>
</tr>
<tr>
<td></td>
<td>4.0</td>
<td></td>
</tr>
<tr>
<td></td>
<td>10.8</td>
<td></td>
</tr>
<tr>
<td></td>
<td>11.3</td>
<td></td>
</tr>
<tr>
<td></td>
<td>13.8</td>
<td></td>
</tr>
<tr>
<td></td>
<td>12.5</td>
<td></td>
</tr>
<tr>
<td></td>
<td>15.7</td>
<td></td>
</tr>
<tr>
<td></td>
<td>14.7</td>
<td></td>
</tr>
<tr>
<td></td>
<td>11.3</td>
<td></td>
</tr>
<tr>
<td></td>
<td>10.8</td>
<td></td>
</tr>
<tr>
<td></td>
<td>11.3</td>
<td></td>
</tr>
<tr>
<td></td>
<td>14.7</td>
<td></td>
</tr>
</tbody>
</table>

Note: By region, the north is the Red River Delta of 11 city provinces, including Hanoi, Haiphong, Bac Ninh and Han Nam Provinces, etc., and the south is defined as six cities and provinces, including Ho Chi Minh City, Dong Nai, Baia Vung Tau, and Binh Duong, etc. Source: GSOV website and the Statistical Yearbook of Viet Nam (each year’s edition).

(2) Direct effects of FDI

Table 5.2 shows the direct impact of FDI in Viet Nam on the country’s economy since 1995. FDI’s contribution to GDP nearly tripled from 6.3% in 1995 to 19.5% in 2020, and FDI’s share of industrial production reached 40% in 2010 (when figures were available). The share of FDI in Viet Nam’s economy is increasing yearly, and it is also shown that FDI is driving Viet Nam’s industrialization.

Although not shown in Table 5.2, the number of domestic enterprises in 2019 was 668,503, with state-owned enterprises accounting for 0.3%, non-state-owned enterprises accounting for 96.9%, and FDI companies accounting for 2.8%. Of these FDI companies, 85.7% were 100% foreign-owned.
Meanwhile, the share of employees working in FDI companies increased to 19.6% in 2005 and 32.8% in 2019. FDI, which accounts for only 2.8% of the total number of companies, accounts for 32.8% of employment, indicating that it has a large job creation effect.

In addition, in terms of domestic investment, FDI increased by 30.4% in 1995. FDI was the second-largest player after the state-owned sector, but as of 2020, the state-owned sector accounted for 33.7%, the private sector 44.9%, and FDI 21.4%, indicating that Viet Nam’s private sector has grown. Viet Nam’s state-owned sector accounts for key industries such as energy, aviation, and chemicals, whilst the private sector mostly comprises small and medium-sized enterprises (SMEs). Transactions through the market with FDI companies also provide potential receptacles for inter-industry spillovers in the private sector, which accounts for about 97% of companies.

FDI’s share of trade has been rising over the years, accounting for 72.3% of exports and 64.3% of imports in 2020. This is because export-oriented and labour-intensive FDI, such as smartphones and tablet PCs, is carrying out large-scale production for the global market in Viet Nam, and imports of the parts and materials necessary for export production have increased. Viet Nam occupies a part of the global supply chain for these ICT-related products, indicating that Viet Nam has become a production area responsible for the horizontal division of labour within the industry.

We have seen how FDI has had a direct impact on Viet Nam’s economy and confirmed that the presence of FDI in Viet Nam’s employment, industrial production, and trade has been rising year by year. If Viet Nam continues to develop economically in the future, its cheap and high-quality labour force may lose its comparative advantage, and FDI in industries with high wage rates, such as clothing, footwear, and furniture, may be transferred to other countries. However, if it is possible to achieve the internationally competitive production of intermediate goods, it will be possible to further sustain and upgrade industrialisation. To this end, local Vietnamese enterprises must find opportunities to trade with FDI and engage in the production of FDI, which produces intermediate goods, and to make progress to the third and fourth steps, as shown in Figure 5.2. The time has come to move forward with industrialisation through the backward linkage from the labour-intensive production of final goods to consolidating equipment and technology-intensive intermediate goods.
### Table 5.2. Changes in the Ratio of FDI to Viet Nam's Major Economic Indicators (%)

<table>
<thead>
<tr>
<th>Year</th>
<th>GDP</th>
<th>Industrial production</th>
<th>No. of enterprises</th>
<th>Employees</th>
<th>Domestic Investment</th>
<th>Net income</th>
<th>Export</th>
<th>Import</th>
</tr>
</thead>
<tbody>
<tr>
<td>1995</td>
<td>6.3</td>
<td>25.1</td>
<td>0.1</td>
<td>na</td>
<td>30.4</td>
<td>na</td>
<td>27.0</td>
<td>18.0</td>
</tr>
<tr>
<td>2000</td>
<td>13.3</td>
<td>35.9</td>
<td>3.6</td>
<td>na</td>
<td>18.0</td>
<td>na</td>
<td>47.0</td>
<td>27.8</td>
</tr>
<tr>
<td>2005</td>
<td>15.2</td>
<td>37.3</td>
<td>3.3</td>
<td>19.6</td>
<td>14.9</td>
<td>na</td>
<td>57.2</td>
<td>37.1</td>
</tr>
<tr>
<td>2010</td>
<td>15.2</td>
<td>41.2</td>
<td>2.6</td>
<td>21.4</td>
<td>25.8</td>
<td>35.2</td>
<td>54.2</td>
<td>43.6</td>
</tr>
<tr>
<td>2015</td>
<td>17.0</td>
<td>na</td>
<td>2.7</td>
<td>29.3</td>
<td>23.3</td>
<td>44.4</td>
<td>70.6</td>
<td>58.6</td>
</tr>
<tr>
<td>2020</td>
<td>19.5</td>
<td>na</td>
<td>2.8(*)</td>
<td>32.8(*)</td>
<td>21.4</td>
<td>45.6(*)</td>
<td>72.3</td>
<td>64.3</td>
</tr>
</tbody>
</table>

**Note:** Figures marked with an asterisk (*) are for 2019.

**Source:** GSOV website and the Statistical Yearbook of Viet Nam (each year’s edition).
4. FDI and Industrialisation in Viet Nam

4.1 Intra-industry Spillovers

The rise in the capital equipment ratio of the Vietnamese manufacturing industry, which had an advantage in the labour force amongst the comparative production costs, indicates that there are labour savings and improvements in production efficiency due to mechanisation.

Table 5.3 shows the ratio of FDI to the value of industrial production in Viet Nam and the rate of increase in the capital equipment ratio. The capital equipment ratio is the fixed asset amount for each industry divided by the number of employees, and it shows the rate of change over the 10 years between 2005 and 2015.

FDI’s share of manufacturing output rose from 36.1% in 2005 to 42.8% in 2010. Industries with a high ratio of FDI were ICT-related products (93.6%), automobiles (77.1%), leather goods (72.5%), and motorcycles (71.9%). Looking at changes in the capital equipment ratio in these industries, ICT-related products increased by 9.6%, automobiles decreased by 19.6%, leather goods increased by 11.9%, and motorcycles increased by 36.7%. Compared to a growth rate of 53.7% in the manufacturing industry as a whole, capital consolidation in industries with a high ratio of FDI was relatively sluggish, and some industries were negative. Intra-industry spillovers have not had a positive effect on capital equipment ratios. On the other hand, the capital equipment ratio rose significantly in industries with a low FDI production ratio, such as base metals, tobacco, and wood products.
Table 5.3. FDI/Industrial Production and the Growth Rate of Capital Equipment Ratio (%)

<table>
<thead>
<tr>
<th>Manufacturing</th>
<th>FDI/Industrial production</th>
<th>Growth of capital equipment ratio</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2005</td>
<td>2010</td>
</tr>
<tr>
<td>Food products</td>
<td>36.1</td>
<td>42.8</td>
</tr>
<tr>
<td>Beverages</td>
<td>24.4</td>
<td>32.5</td>
</tr>
<tr>
<td>Tobacco products</td>
<td>38.7</td>
<td>34.5</td>
</tr>
<tr>
<td>Textiles</td>
<td>0.8</td>
<td>2.1</td>
</tr>
<tr>
<td>Wearing apparel</td>
<td>30.6</td>
<td>36.6</td>
</tr>
<tr>
<td>Leather and related products</td>
<td>59.4</td>
<td>72.5</td>
</tr>
<tr>
<td>Wood and products of wood and cork</td>
<td>17.8</td>
<td>11.2</td>
</tr>
<tr>
<td>Paper and paper products</td>
<td>18.4</td>
<td>30.3</td>
</tr>
<tr>
<td>Chemicals and chemical products</td>
<td>46.3</td>
<td>58.9</td>
</tr>
<tr>
<td>Pharmaceuticals, medicinal chemical and botanical products</td>
<td>19.9</td>
<td>42.6</td>
</tr>
<tr>
<td>Rubber and plastics products</td>
<td>29.0</td>
<td>39.4</td>
</tr>
<tr>
<td>Other non-metallic mineral products</td>
<td>23.9</td>
<td>26.9</td>
</tr>
<tr>
<td>Basic metals</td>
<td>34.2</td>
<td>29.5</td>
</tr>
<tr>
<td>Fabricated metal products</td>
<td>35.6</td>
<td>40.4</td>
</tr>
<tr>
<td>ICT-related products</td>
<td>86.6</td>
<td>93.6</td>
</tr>
<tr>
<td>Electrical equipment</td>
<td>42.2</td>
<td>46.2</td>
</tr>
<tr>
<td>Automobiles</td>
<td>79.2</td>
<td>77.1</td>
</tr>
<tr>
<td>Other transport equipment</td>
<td>63.7</td>
<td>71.9</td>
</tr>
<tr>
<td>Furniture</td>
<td>35.9</td>
<td>35.3</td>
</tr>
</tbody>
</table>

Notes:
1. The capital equipment ratio is set at 100 (baseline) in 2005, and the Consumer Price Index increase rate up to 2015 is set at 237.61 as a deflator to make the prices real.
2. The item name ‘computers, electronics, and optical equipment’ is described as ICT-related products, and ‘other transportation equipment’ is described as motorcycles.

4.2. Inter-industry Spillovers

We examine the effects that have resulted from the backward and forward linkages with industries that have embraced FDI. First of all, in the process of industrialisation, supporting industries are needed and nurtured only with the development of the downstream industries that utilise them. For this reason, in the export-oriented manufacturing sector with a high FDI ratio, it is considered that the backward linkage has a greater effect than the forward linkage effect.

Table 5.4 shows changes in Viet Nam’s trade structure by production process, classified based on the input-output table. In 2000, the total value of consumption goods and primary goods accounted for 87.0% of the total export value, and processed goods accounted for 53.8% of imports. According to customs statistics, Viet Nam’s exports in 2000 were mainly light industrial goods such as clothing and footwear, as well as primary products such as crude oil, marine products, coffee, tea, spices, and rice. The main imports were petroleum products, such as gasoline, steel, plastics, and textiles. At that time, the import-substitution type of FDI was the mainstream in Viet Nam. The trade conditions for exports were not yet developed, and FDI, which plays a part in the global supply chain of multinational companies, had not yet entered Viet Nam. Therefore, in the trade structure, primary products and light industrial products (consumer goods) such as clothing and footwear were the main export products, and processed products (intermediate goods) were the main import products.

Subsequently, the export structure in 2020 showed a decline in the share of primary goods and consumption goods, and an increase in exports of capital goods and intermediate goods (parts and components, and processed goods). On the other hand, the share of parts and components in imports more than doubled, indicating an increase in imports of intermediate goods for export production. It is probable that the increase in imports and exports of intermediate goods was attributable to the horizontal progress of the international division of labour. In Viet Nam’s industrial production, the industries with a high ratio of FDI were ICT-related products, automobiles, leather goods, and motorcycles, etc. Viet Nam’s automobile industry is an import substitution industry with almost no exports. In addition, the manufacture of leather products comprises importing raw hides, processing them in Viet Nam, and exporting them, and the supply chain has a relatively simple structure. Therefore, using the trade specialisation coefficient (TSC), we will consider smartphones, which have a large export share amongst ICT-related products, and motorcycles, which started as an import substitution industry but whose import restrictions did not work.

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10 According to UN Comtrade, the value of exports of passenger cars, commercial vehicles, and other finished vehicles in 2019 was US$55.3 million, and the export volume was 2,879 units, whilst the import value was US$3,216.25 million, and the import volume was 147,385 units.
Table 5.5 shows the TSC of the final goods and parts of these two items. The TSC is an index of the trade balance, where 1.0 indicates export specialisation, -1.0 indicates import specialisation, and 0 indicates the export-import equilibrium or lack of trade. According to Table 5.5, the TSC of both finished products of motorcycles and parts of motorcycles were at a level close to import specialisation in 2000. Later, however, as the TSC of the finished products increased, the TSC of the parts also increased. In 2020, Viet Nam became a net exporter with international competitiveness in both finished motorcycles and parts for motorcycles.

As for smartphones, since 2015, finished products have almost reached the level of export specialisation, and the TSC of parts has risen from a negative level to turn positive in 2020. In the case of motorcycles and smartphones, along with the expansion of exports of finished products, the export of domestically produced parts has also begun, and it has been found that the trade balance has become profitable. These industries suggest that the backward linkage effect of FDI, which produces final goods on a large scale, has led to the industrialisation of parts production in the previous process.

### Table 5.4. Changes in Viet Nam’s Trade Structure

<table>
<thead>
<tr>
<th></th>
<th>Exports</th>
<th></th>
<th>Imports</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Final goods</td>
<td>Capital goods</td>
<td>2.1</td>
<td>9.7</td>
<td>26.0</td>
</tr>
<tr>
<td></td>
<td>Consumption goods</td>
<td>54.0</td>
<td>53.7</td>
<td>35.8</td>
</tr>
<tr>
<td>Intermediate goods</td>
<td>Parts &amp; components</td>
<td>4.5</td>
<td>8.2</td>
<td>21.3</td>
</tr>
<tr>
<td></td>
<td>Processed goods</td>
<td>6.4</td>
<td>12.5</td>
<td>13.1</td>
</tr>
<tr>
<td>Primary goods</td>
<td>Primary goods</td>
<td>33.0</td>
<td>15.9</td>
<td>3.8</td>
</tr>
</tbody>
</table>


### Table 5.5. Changes in the Trade Specialisation Coefficient (%)

<table>
<thead>
<tr>
<th></th>
<th>Motorcycles</th>
<th></th>
<th>Smartphones</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Finished products</td>
<td>▲ 1.0</td>
<td>▲ 0.3</td>
<td>▲ 0.3</td>
<td>0.7</td>
</tr>
<tr>
<td>Parts</td>
<td>▲ 0.8</td>
<td>▲ 0.6</td>
<td>▲ 0.1</td>
<td>0.3</td>
</tr>
</tbody>
</table>

Source: UN Comtrade.
5. Conclusion

5.1. The Role of FDI in Industrialisation

This study has discussed the role that FDI played in Viet Nam’s economic development. With regard to the horizontal intra-industry spillover effect from the perspective of indirect effects, it was confirmed that the capital equipment ratio stagnated in industries with a high FDI ratio and became relatively labour-intensive. The reasons why capital concentration has not progressed in the industries in which FDI has entered are: (1) labour-intensive assembly processes still have a comparative advantage; (2) new capital investment is stagnant in import substitution industries, such as automobiles; and (3) it is possible that there are no local companies in the industry that compete with FDI, or that technical disparities are large and they are not subject to spillovers.

If so, for Viet Nam’s industrial spillover, we must wait for the fourth step shown in Figure 5.2, i.e., the emergence of local companies that have international competitiveness and compete with FDI in Viet Nam. In order to enhance the competitiveness of final goods, it is necessary to accumulate a wide range of intermediate goods. This requires a further deepening of the third step, in which local companies are involved in the production of intermediate goods with international competitiveness.

Next, with regard to inter-industry spillovers, domestic demand industries could not be considered because trade data was used. However, with regard to external demand industries, it was confirmed that Viet Nam is actively promoting the horizontal division of labour amongst intermediate goods. In the smartphone and motorcycle industries, which are representative items, exports of intermediate goods increased as if chasing the export of final goods. It was suggested that industrialisation spread from labour-intensive processes to capital- and technology-intensive intermediate goods production processes due to backward linkage effects.

5.2. The Role of Japan’s FDI in Viet Nam’s Development

I would like to consider the role played by Japan’s FDI in Viet Nam’s industrialisation. According to Japan’s balance of payments statistics, the amount of outward FDI from Japan was ¥190.4 trillion at the end of 2020, with the manufacturing sector accounting for 41%. These investment destinations were North America (32%), Asia (29%), and Europe (27%). The breakdown of Asia was China (33%), Thailand (17%), Singapore (9%), India, Korea, and Indonesia (7% each), and Viet Nam (4%). Viet Nam opened its markets to foreign capital later than other Asian countries. However, in terms of the scale of Japanese FDI, it exceeds that of the Philippines and Malaysia. In addition, 61% of Japan’s investment in Viet Nam was in the manufacturing sector.

Now, I would like to express my personal opinion on the role Japan’s FDI played in Viet Nam’s industrialisation. First, as already mentioned, Viet Nam’s acceptance of FDI in the manufacturing sector from the mid-1990s to the mid-2000s was preceded by import-substitution industries, such as automobiles, televisions, and motorcycles. The import and substitution type FDI of these durable consumer goods was mainly in the manufacturing industry of Japan, with firms such as Toyota, Honda, Suzuki, Yamaha, Matsushita Electric, Sony, and JVC. The substitution of imports through protectionism may not have been a desirable policy, but it is also true that it brought about
certain results in Viet Nam at a time when the trade environment through free trade had not yet been acquired. For example, it should have had positive direct effects, such as job creation, the utilisation of the management resources of unprofitable state-owned enterprises, and the transfer of corporate management know-how, international marketing skills, and production and mass production technologies to the Vietnamese side.

Secondly, FDI by Japanese companies in the field of industrial park development was carried out in northern Viet Nam in the mid-1990s ahead of other countries. As mentioned, the Thang Long Industrial Park in Hanoi and the Nomura Haiphong Industrial Park in Haiphong were opened in the late 1990s. At that time, southern Viet Nam was preferred to northern Viet Nam due to disparities in the economic level, number of private companies, and infrastructure development, etc., and there was little FDI for manufacturing in the north, except for import substitution companies. Although there was a need for a production site for the FDI manufacturing industry in northern Viet Nam, few foreign-invested companies wanted to proceed with the development of industrial parks. Under these circumstances, it is significant that Japan was able to develop an industrial park with a long-term vision in cooperation with highway development and port development through official development assistance. At the time of the Asian currency crisis and recession, Canon, a major Japanese precision equipment manufacturer, was able to expand into northern Viet Nam because there was an industrial park that could accept large-scale export-oriented manufacturing. Viet Nam’s subsequent rush to enter export-oriented FDI has continued to this day, in step with the expansion of Viet Nam’s free trade environment.

The role played by Japanese FDI in the ‘import substitution period’ and the ‘structural reform period’ shown in Figure 5.3 was significant, and by going through this phase, Viet Nam was able to develop into the ‘export-oriented period’ and the ‘making a leap period’.
5.3. Policy Recommendations

Finally, I would like to try to make policy proposals to link the economic activities of FDI in Viet Nam to the country’s further industrialisation. Viet Nam’s steady economic development has gradually reduced the comparative advantage of its workforce, and it is necessary to transform its leading industries from labour-intensive industries, such as assembly, to industries that require capital and technology. As confirmed in this chapter, Viet Nam has acquired the intermediate goods production process due to the backward linkage effect from the large-scale production process of final goods by FDI. At present, it is important to diversify the production of intermediate goods and develop them into competitive industries.

(1) Development of Supporting Industries

As shown in Figure 5.2, in the third step, in which local firms enter the production of intermediate goods, the production of intermediate goods needed the supporting industries with fundamental technologies, such as molds, castings, surface treatment, sheet metal, welding, and heat treatment. Since it is also FDI companies that produce the parts and components required for the production of final products, local companies will participate in the supply chain in collaboration with these FDI companies. How to encourage this will be an urgent issue.

The Vietnamese government also seems to have sufficient awareness of these issues, and, in fact, it is showing active measures to foster local companies. For example, the SME Support Act, which came into effect in 2018, clarified the responsibilities of the supporter (administrative side) and attracted attention as a foundation law for effective support for SMEs. Article 19 of the Act stipulates support measures for Vietnamese SMEs to participate in the value chain, including consulting, information provision, brand development support, the issuance of prototype and inspection certificates, and interest subsidies. In August 2020, the government enacted Resolution No. 115 (115/NQ-CP), which set out stronger support measures than before for measures to foster supporting industries. According to the Resolution, the target fields are electronics, automobiles, textiles and sewing, leather, and high-tech industries, etc., and by 2025, the target is to achieve an increase in domestic procurement to 45%, 11% of industrial production value, and 300 local enterprises to participate in the global supply chain of multinational corporations. In addition, the Resolution stipulates that five supporting industrial technical support centres in major regions of Viet Nam will be established, interest rate subsidies will be provided to supporting industrial enterprises, large-scale FDI will be attracted, and opportunities for local companies to enter the market will be created (Chinhphu.vn).

(2) Matching Support

In addition to such progress in the development of legislation, events have been held to provide opportunities for business negotiations between companies as a concrete support measure. For example, since 2010, Japan has been holding parts procurement exhibition business meetings in Viet Nam, called the Japan-Viet Nam Supporting Industry Show, providing opportunities for matching local companies in Viet Nam with Japanese companies. In September 2021, the ninth exhibition and business meeting was held in an online format, with 20 Japanese companies and
35 Vietnamese companies participating from industries including automobile and motorcycle-related parts, electrical and electronic parts, mechanical parts, metal and resin processing (casting, forging, injection molding, molding, sheet metal, press processing, plastic processing, and plating treatment, etc.), and packaging materials, etc.

In addition, in 2020, the Vietnam International Supporting Industry & Manufacturing Exhibition (VIMEXPO), organised by the Ministry of Industry and Trade of Viet Nam, was held, and in December 2021, the second time the exhibition was held, 170 companies including major Vietnamese companies and FDI participated. In this way, the Vietnamese government is also actively providing opportunities for exchange and matching between FDI and local companies. In other words, these support measures are in the third step of industrialisation as shown in Figure 5.2, and they are important in supporting the internalisation of internationally competitive intermediate goods production. In fact, the production of a wide variety of intermediate goods through FDI has already begun in Viet Nam, and the conditions are being prepared for local companies to enter the production of intermediate goods.

In addition, equipment for producing parts and materials for large-scale FDI is often a related specific investment. For Vietnamese SMEs, such special investment is a risk, and they have no choice but to hesitate to make capital investments. In order to enable firms to make such capital investments with peace of mind, it is desirable to reduce the investment risks of Vietnamese companies by subsidising not only low-interest loans but also capital investment itself.

3) Support for Building Vietnamese Brands

With regard to support for the fourth step of Figure 5.2, large firms with financial resources will basically be the first players amongst local firms. Vingroup has already made new entries into the fields of ICT-related products, automobiles, and electric vehicles. Although it is premature to judge the success or failure of Vingroup’s entry into the electric vehicle market, it is necessary for the government to support the emergence of other companies similar to Vingroup and establish a local brand in Viet Nam that will launch itself in the global market. This is because it is the strong production of final goods that will enhance the production of intermediate goods through the backward linkage effect and strongly drive Viet Nam’s industrialisation.

Although the target of the support may be large enterprises with financial power in Viet Nam, the required capital investment, market research, and building of dealerships to challenge the global market are enormous and will require public backing in addition to funding from the stock market. In addition to providing financial support, such as low-interest loans and interest rate subsidies, to companies that are taking on challenges in the global market, the introduction of a trade insurance system that provides a certain degree of guarantee for export and local production for markets with high country risk will be effective support measures.
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