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Investment climate in Vietnam: potentials and limitations

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Abstract

Due to economic renovation in 1986, Vietnam has gained a number of convincing social-economic achievements. One of the factors determining the success of Vietnam's economy is the support of foreign direct investment. Thus, the study and analysis of the determinants, affecting the ability to attract foreign investment have become more practically oriented and necessary. The main purpose of the article is to clarify the definition of *investment climate* and its characteristics in Vietnam. The article demonstrates several advantages and potentials in the investment climate of Vietnam. It also figures out some limitations and problems to be eliminated to enhance competitiveness of Vietnam for foreign direct investment (FDI).

Keywords: foreign direct investment (FDI), investment climate, investment environment, potentials, limitations, attraction

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1. Introduction

Globalization is a popular term in the last decade. It is the way to economic, political and cultural integration of the world. The clearest sign of globalization is foreign direct investment (FDI) growth. Recently, foreign direct investment has been regarded as an important motivating factor for economic development. Obviously, FDI brings many benefits, such as human capital development, acquisition of new technology, solution of the problem of unemployment, contribution to international trade integration and so on. Due to the importance of FDI for economic development, Vietnam focuses on creating the ideal environment to attract capital of foreign investment. Creating attractive investment environment is a process of discovering and promoting the existing potentials, at the same time eliminating the difficulties and limitations having bad impact on the ability to attract foreign investment.

2. Main part

In 1986, the Sixth Congress of the Vietnamese Communist Party implemented the first set of renovation policies referred to as “doi moi” (the name given to the economic reforms with the goal of creating a "socialist-oriented market economy"). According to “doi moi”, Vietnamese economy was converted to an open, liberalized, market-oriented, and globally integrated model [2]. Due to this reform, annual foreign direct investment inflows into Vietnam have increased dramatically from 0.32 million USD in 1988 [6] to nearly 1.837 billion USD in the first quarter of 2015 from foreign investors [3]. According to the Report of Foreign Investment Department, only in the first quarter of 2015, investment certificates have been granted to 267 projects of FDI. Data of the foreign partners' investment proportion in Vietnam are shown in the following pie chart:

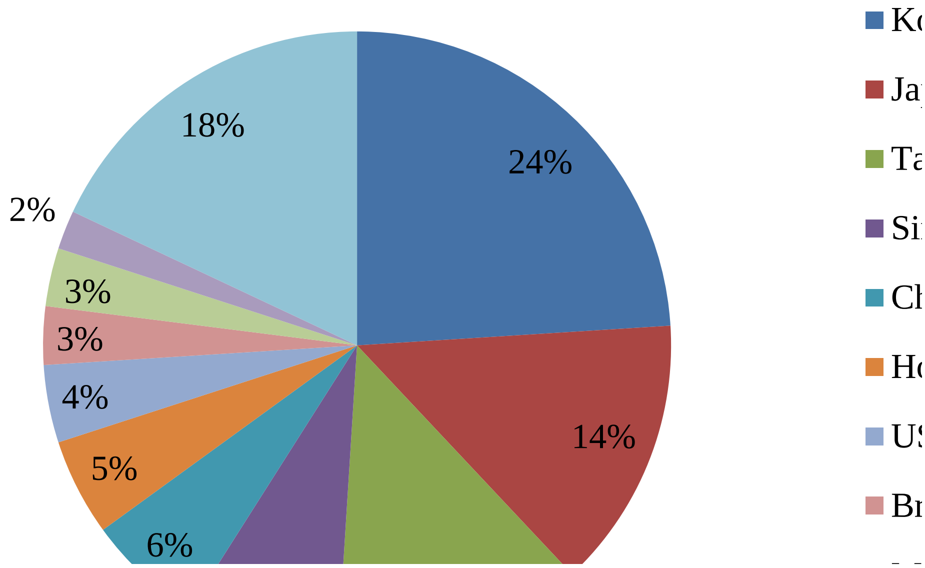

Chart 1. Proportion of FDI projects by investment partners accumulated as of March 20, 2015[4].

So far, investors from different countries are investing in Vietnam, but Asia accounts for about 60% of FDI projects proportion by all Vietnamese investment partners. Korea is the biggest foreign investor occupying 24%, followed by Japan, Taiwan, Singapore and China. It should be noted that Asian countries tend to invest in Vietnam not only because Vietnam is located in the center of Southeast Asian region, which makes it so convenient for transaction, but also because Vietnam has an ideal investment climate considering a key factor for attracting foreign direct investment.

Investment climate is the institutional, policy, and regulatory environment in which a firm operates. Key determinants of the investment climate include economic and political stability, rule of law, infrastructure, approaches to regulations and taxes, functioning of labor and finance markets, and broader features of governance [1]. The desire of investors to put their capital in the business of another country depends on existence of these factors in its investment climate. Due to the importance of *investment climate* for attracting FDI, Vietnam always strives to maintain their strengths and overcome the weaknesses existing in this investment environment.

Nowadays, Vietnam is regarded as a country with great potentials for economic development and high competitiveness in attracting foreign investment capital.

Firstly, one of the most important factors in shaping the investment climate in Vietnam is its openness and integration capabilities. In recent years, Vietnam has entered many international economic organizations, such as ASEAN (Association of Southeast Asian Nations, 1995), APEC (Asia-Pacific Economic Cooperation, 1998), WTO (World Trade Organization, 2007) etc. Membership in these organizations brings Vietnam an opportunity to expand cooperation with other countries and attract investments from them. It is noteworthy that in 1995, Vietnam joined the Multilateral Investment Guarantee Agency (MIGA), Vietnam has 58 bilateral investment treaties with different countries, such as Argentina, Austria, China, France, Germany, India, Italy, Japan, Russia, Singapore, South Korea, etc [8].

Secondly, Vietnam has abundant natural resources (gas, bauxite etc.) and high capacity of the internal market. Market size can have a significant impact on the level of economic development measured by the GDP per capita. Economic growth in Vietnam in 1991-2010 averaged 7.5% a year and, in spite of the economic fluctuation and many difficulties the country faced between 2011 and 2013, GDP growth still rose by 5.6% [7].

Thirdly, Vietnam enjoys the reputation of the safest country in the region, because the government always attempts to provide the social and political stability. In Vietnam, there are fewer problems related to religious discrimination, languages or ethnic disputes, and the safety of foreign direct investments is guaranteed. Moreover, the attractive investment climate in Vietnam gradually develops due to building an advanced and integrated infrastructure, developing a quality workforce, improving the relevant legal framework and institutions related to business and investment, so that the competitiveness of investment climate in Vietnam will be enhanced. For instance, the Law on Foreign Direct Investment has been first promulgated in December 1987 and since then it has been amended several times (in 1990, 1992, and 1996, 2000, 2005, 2014), responding to the needs of the investors [8]. Vietnam also created laws and regulations designed to protect foreign property, ensure its integrity. In case of law amendments, the government is obligated to compensate their losses. These measures have positive affect on FDI.

Furthermore, such characteristics of labor market as labor cost, availability, and productivity can affect the level of competitiveness of developing countries in attracting FDI. The cheaper the labor is, the larger the FDI inflows are. Fortunately, Vietnam is currently in a period of golden population structure – more than 60% of its population are working age [7]. It leads to the low cost of labor there.

In addition, Vietnam maintains close connection with the Vietnamese diaspora community (Viet kieu). One of the most important potentials of Viet kieu is considered to be a source of money invested in large projects in Vietnam. A bridging role of the Vietnamese Diasporas in international cooperation was also promoted, which contributes to technology transfer, investment and development in chemistry, microbiology, photoconductive, information technology [5].

To sum up, these factors partially explain why so many choose to invest in Vietnam. However, there are some disadvantages and restrictions in investment policies of the government. For example, bureaucracy affects the process of project implementation. In some situations, investors even have to give bribes to the officials in other to get a license to launch their projects legally. Thus, corruption of public officials is one of the biggest restrictions on investment policies of government and unsolvable challenge of the Vietnamese economy [5].

What is more, relationships between the government and business are loose, banking and financial system is quite weak. Besides, high costs of running business such as cost of international telephone calls, Internet fees, and seaports are the first disadvantage for the foreign investor. Corporate Tax and Personal Income Tax (50% of the gross income) are well above average within the region. Infrastructure in Vietnam has been up-graded generally but the quality of some public goods and services is not very high [8].

To deal with these problems, Vietnamese government should cancel the local content requirement. The law fees need to be cut off. The bureaucracy of public administration and the complexity of legal procedure must be reduced. In 2005, Vietnamese anticorruption Law was issued to fight against bribery among public officials in international business transactions. On the other hand, Vietnam should develop technologies, improve training of the staff, labour efficiency, up-grade the development of infrastructure and create an environmentally friendly *investment climate*. Especially, summoning Vietnamese living abroad to invest in the country's growth is one of the important policies of Vietnamese government.

3. Conclusion

Generally, in technologies the analysis of factors of investment climate attractiveness, it is proved that Vietnam has successfully attracted large volumes of foreign direct investment (FDI) due to plenty of potentials and advantages of investment environment there. They are the integration and successful cooperation between Vietnam and the others countries especially the Asian ones having similarities in culture, history and common goal of economic development in their region, the wealth of natural and labor resources, social and political stability and preferential policies to attract foreign direct investment. However, there are some negative factors decreasing the ability to attract FDI, as well as the economic development of this country. Therefore, the Vietnamese government must strive to maintain the advantages, reduce existing negative aspects to improve investment environment, and attract as much capital from foreign investors as possible.

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