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VIETNAM'S INTERNATIONAL ECONOMIC INTEGRATION: CURRENT SITUATION AND POLICY ORIENTATION

International economic integration has been a driving force of Vietnam's growth since Vietnam introduced Doi Moi policy (Renovation) in 1986. This paper focuses on analysing two important aspects of Vietnam's economic integration, i.e. trade and investment relations between Vietnam and other countries using various trade and investment databases (Vietnam's General Statistics Office, General Department of Vietnam's Customs, and UN's COMTRADE). Study findings show that there have been long-term challenges for Vietnam's trade structure such as main share of low value of export goods, persistent trade deficit, and main share of import comes from intermediate goods. As for FDI, there is concern on its quality since knowledge-based sectors, such as health, education, training, science and technology, finance, banking and insurance are only modest. Some policy recommendations are put forward to improve trade structure and FDI quality for long-term growth.
JEL: F15; F21

1. Introduction

Economic integration and institutional transformation from a centrally planned model to a market economy are the two most significant factors that explain the growth of Vietnam in the past 30 years of Reform. While institutional transformation into a market economy has freed social resources and promoted private sector development, the process of integration with the world and regional economy has connected Vietnam with the world through FDI attraction, technology import, export markets' expansion, and domestic institutional change. As a result, growth is enhanced.

Within the framework of this article, the author will be providing an overview of the trade and investment relations between Vietnam and other countries, which are the two most important issues in Vietnam's economic integration, and a number of policy orientations in the future.

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2. Vietnam's integration channels

Vietnam entered into the first FTA with ASEAN in 1995, then signed BTA with the US in 2000, acceded into the WTO in 2006, and signed a number of bilateral FTAs. Vietnam has carried out simultaneously three channels of integration, namely, regional, multilateral, and bilateral channels.

Table 1

Integration channels of Vietnam economy

Channel	Member	Status
Regional		
AFTA	10 ASEAN countries	Signed in 1992 (ASEAN-6), Vietnam participated in 1995, the other countries joined AFTA later.
ASEAN-China	10 ASEAN countries and China	Signed in 2004
ASEAN-Japan	10 ASEAN countries and Japan	Signed in 2008
ASEAN-South Korea	10 ASEAN countries and South Korea	Signed in 2006; Thailand joined in 2009
ASEAN-India	10 ASEAN countries and India	Signed in 2009
ASEAN-Australia-New Zealand	10 ASEAN countries, Australia and New Zealand	Signed in 2009
Trans-Pacific Strategic Economic Partnership Agreement (TPP)	12 countries: Vietnam, Australia New Zealand, Singapore, Brunei, Malaysia, Japan, Chile, Peru, the United States, Mexico, Canada	Finished the October 2015 negotiation
EAFTA (ASEAN+3)	10 ASEAN countries, China, Japan, and South Korea	Negotiating
Multilateral		
WTO	Became the 150th member	Acceded in 2007
Bilateral		
Vietnam – The US	Vietnam and the US	Signed in 2000
Vietnam – Japan	Vietnam and Japan	Signed in 2008
Vietnam – Chile	Vietnam and Chile	Signed in 2011, took effect in 2014
Vietnam – South Korea	Vietnam and South Korea	Signed in May, 2015
Vietnam – Eurasian Economic Union (EEU)	Vietnam – 5 EEU member countries (Russia, Belarus, Kazakhstan, Armenia, and Kyrgyzstan)	Signed in May, 2015
Vietnam – EU	Vietnam and EU	Finished negotiations in August, 2014
Vietnam - EFTA	Vietnam and 4 countries including Switzerland, Norway, Iceland and Lichteinsten	Negotiating

Source: from different sources.

In terms of regional integration, following AFTA, which Vietnam became a member in 1995, ASEAN and China free trade agreement was signed in 2004. In addition to directly signed free trade agreements (FTA), as a member of ASEAN, Vietnam has indirectly integrated with other economies via ASEAN. Through ASEAN, Vietnam also indirectly signed FTA with South Korea (2006), Japan (2008), India (2009), Australia and New Zealand (2009).

The most significant milestone of world economic integration was marked when Vietnam acceded into the WTO in 2007. It was the first time that Vietnam participated in a global playground with 150 member states under rigidly binding legal commitments, which require strict compliance from member states. It was also the first time that Vietnam had to adjust its economic institutions in various aspects including trade, investment, intellectual property, etc., to comply with international business practices.

In terms of bilateral integration, Vietnam signed the Bilateral Trade Agreement (BTA) with the US in 2000. This agreement has led to a number of positive results for the economy of Vietnam. It is regarded as an important rehearsing step for the country prior to becoming an official member of the World Trade Organization (WTO) as a number of commitments in BTA employ the WTO approach. Vietnam also signed several bilateral FTAs with other partners such as Japan (2008), Chile (2011), South Korea (2015), and the Eurasian Economic Union (2015).

Vietnam has recently attempted to negotiate some 'new generation' FTAs like the Vietnam – EU or TPP. The negotiation rounds of agreements have been completed, and they are expected to take effect in the near future. With completely new content compared with the previous FTAs, including public procurement labor relations (the role of independent trade unions), and state enterprise, etc., these agreements may have significant impact on the economic institution of Vietnam, and require drastic reform to benefit from opportunities and meet the rigorous demands of other partners.

3. Vietnam trade overview

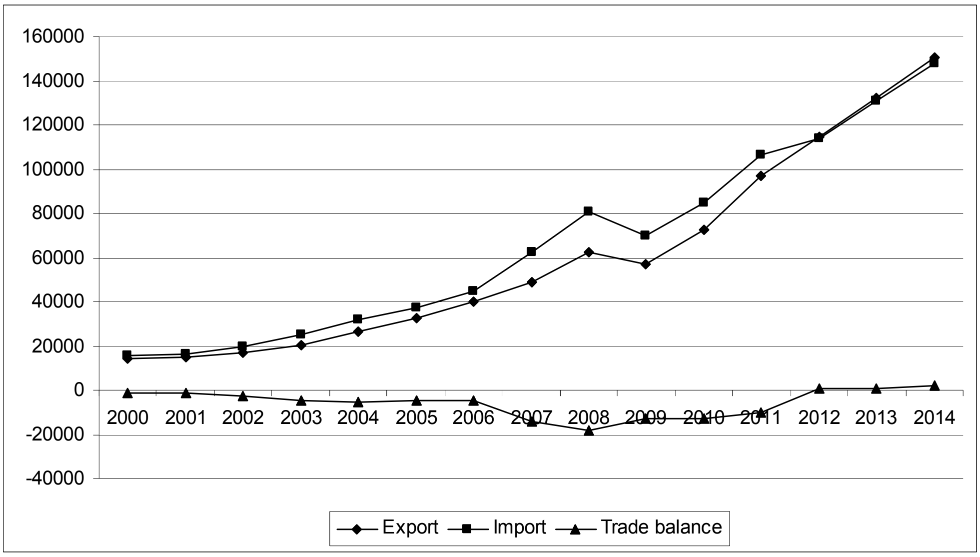
Vietnam is one of the countries that have high economic opening level with a total export and import against GDP rate of 160% in 2014. Trade plays an increasingly important role for economic development, in which export creates jobs, and contributes to budget revenues and foreign currency reserves. In addition, import has a significant implication in creating production input for the economy.

Trade statistics of Vietnam for the 2000-2014 period shows continuously rising trends in both export and import values; except in 2009 under the impact of the global financial crisis, Vietnam trade diminished, but bounced back the following years.

During this period, Vietnam trade balance underwent a deficit, with a growing trade deficit till 2008, then a declining deficit in 2012. Trade became balance in 2013 and witnessed a slight surplus in 2014. The decline in growth of recent years was due to macroeconomic instability, which led to the reduction of input import, thus narrowing trade balance to balanced and slight surplus in the 3 years from 2012 to 2014.

Figure 1

Vietnam Trade, 2000-2014 (mln USD)



Source: Vietnam General Department of Customs.

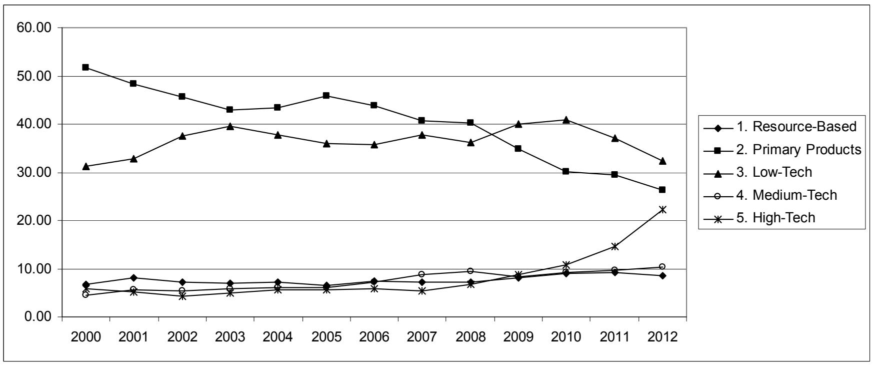
3.1. Export Structure

Export structure by technology level

The proportion of primary products in Vietnam exports saw a decreasing trend from over 50% in 2000 to under 30% in 2012. Goods containing medium and high technology level, particularly high-tech goods, rose sharply in the past 3 years from less than 10% in 2009 to more than 20% in 2012. The primary contribution to the growth of high-tech goods is from the significant increase in export of smart phones produced in Vietnam by Samsung group. The export value of Samsung in Vietnam in 2012 reached USD 12.6 billion, accounting for 11% of total national exports. In 2013, Samsung group continued to be the leading exporter of Vietnam, with the export revenue of USD 23.9 billion, making up 18% of total national exports. However, the current export structure shows a significant proportion of primary products and low-tech goods (textiles, footwear, rice, coffee, or shrimp, etc.) Though high-tech goods underwent a sharp growth, the added value seems small, which remains primarily in the assembly stage in Vietnam of electronic conglomerates like Samsung and Nokia.

Figure 2

Export structure by technology level, 2000-2012 (%)



Source: Author's calculation based on Comtrade database.

Export structure by market

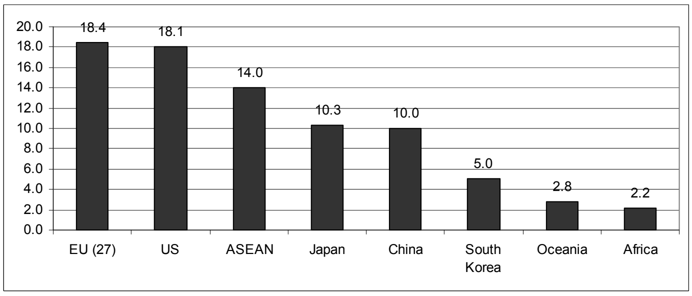
The EU is the largest market for Vietnam's exports, with a proportion of 18%, followed by the US, ASEAN, Japan, China, and South Korea. Other markets import an insignificant amount of Vietnam's goods.

A typical feature of Vietnam's exports to developed countries like the EU, the US, Japan and South Korea is the large proportion of low-tech goods. They are the traditional export items of Vietnam, which requires a large number of labor, for example, textiles, footwear, and wood products. For the EU market, high-tech exports from Vietnam have grown rapidly to a nearly reach the amount of lower tech goods (over 38%), which are primarily cell phones and accessories.

Primary products make up an overwhelming proportion in such markets as China (50%) and ASEAN (30%) with main commodities being crude oil, rubber, coal, other minerals, and agricultural and fishery goods. In these two markets, high-tech goods such as cell phone, computer, and components tend to rise thanks to the efforts of several high-tech trans-national corporations (TNCs) in Vietnam like Samsung, Apple, and Nokia, etc.

Figure 3

Export structure by market, 2013 (%)



Source: Vietnam General Department of Customs.

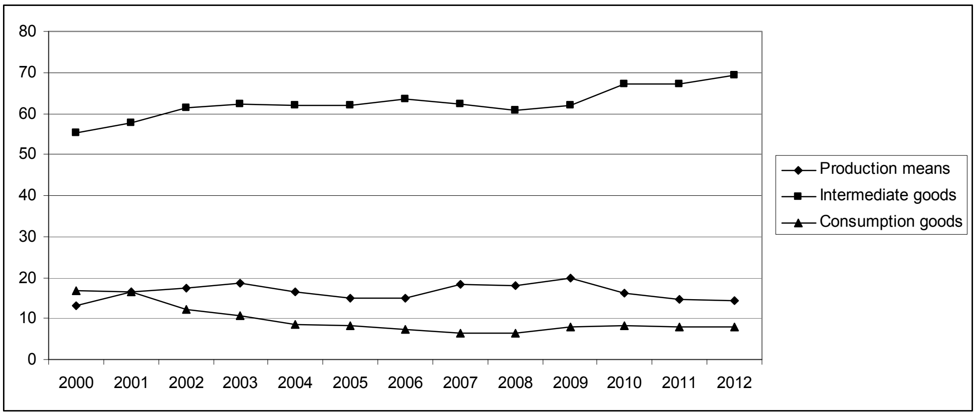
The export values to these major markets saw a swift growth over the years. This shows a deeper integration into the world largest markets of Vietnam. Accession to the WTO is a positive factor to trade. Vietnam exports are no longer discriminated, but enjoy an equal import tariff as other member states in WTO member countries. Accordingly, exports in 2007 and 2008 increased across all markets, and seemed less likely to divert trade under the impact of free trade areas. In addition to traditional markets, Vietnam succeeded in expanding export markets to countries in Africa and Latin America to mitigate the risk of external shock resulted from focusing on certain markets.

3.2. Import Structure

As can be seen from the import structure of Vietnam, the proportion of intermediate goods has grown continuously from 55.1% in 2000 to 69.4% in 2012. Meanwhile, the proportion of consumption goods reduced from 16.8% in 2000 to 7.9% in 2012. Production means accounted for a modest 14.2% in 2012. Therefore, intermediate goods made up a significant proportion, following by production means and consumption goods. This feature of import structure by usage objective fits well with the major import markets of Vietnam, such as China, the EU, ASEAN, South Korea and Japan.

Figure 4

Import structure by usage objective, 2013 (%)

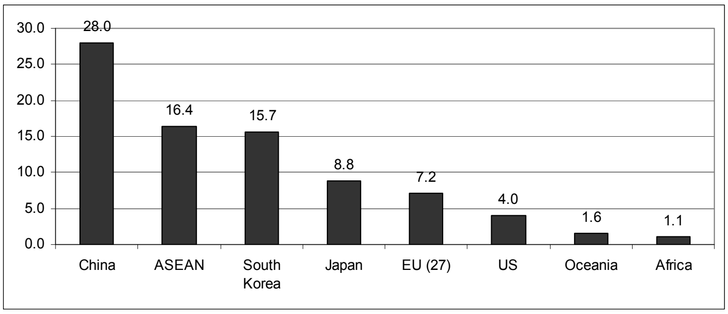


Source: Author's calculation based on Comtrade database.

In terms of market structure, China is the major partner which accounted for 28% of total imports in 2013, followed by ASEAN, South Korea, Japan, the EU and the US. China is also the market where import growth rate is the rapidest, rising by 21 folds between 2000 and 2012. Meanwhile, imports from the US, South Korea, the EU, Japan and ASEAN 6 increased by 13.5 times, 9 times, 7 times, 5 times, and 4.6 times respectively.

Figure 5

Import structure by partner, 2013 (%)



Source: Vietnam General Department of Customs.

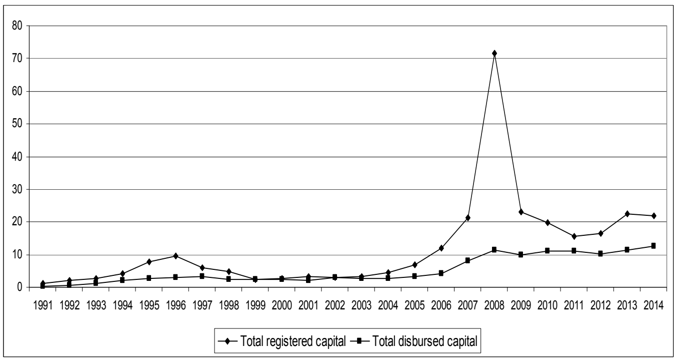
4. FDI in Vietnam

Foreign direct investment (FDI) to Vietnam began when the country issued the Law on Foreign Investment in 1987. As an emerging market with abundant natural resources, cheap labor cost, and relatively large population, Vietnam has attracted a great inflow of FDI over 30 years. The FDI figure for 1991 was only USD 400 million, and went up by 5 times after a year (1995) to reach USD 2.7 billion. From 2008 onwards, the figure remains relatively stable at over USD 10 billion.

History of FDI attraction in Vietnam divides into two periods: 1991-1997 and from WTO accession to now. In the former period, Vietnam succeeded to attract just some big "names" such as BP, Shell, Total (petroleum industry), Daewoo, Toyota, Ford, Honda (automobile, motorcycle), Sony (electronics), Phu My Hung (real estate), but after WTO accession there came more big projects of billions of USD such as chipset project of Intel in Ho Chi Minh City, mobile telephone manufacturing by Nokia in Bac Ninh's VSIP, by Samsung in Bac Ninh and Thai Nguyen provinces, steel project by Formosa in Ha Tinh province, Ho Tram Casino in Ba Ria – Vung Tau, etc.

Figure 6

FDI inflows in Vietnam, 1991-2014 (bln USD)



Source: Vietnam General Statistics Office.

Structure of FDI in Vietnam by economic sectors

Regarding accumulated value of FDI until the end of 2013, ***manufacturing sector*** accounts for the highest share (56%), following by ***real estate service*** (19.1%). For the rest, each sector accounts for less than 5%. Nevertheless, despite an advantage in agriculture of Vietnam, the FDI that goes to agricultural sector accounts for only 1.5%. Other sectors, such as health, education, training, science and technology, finance, banking and insurance are only modestly attractive to foreign investor, portrayed by their share of less than 1% (Table 2).

Table 2

FDI in Vietnam by economic sectors (accumulated till 31.12.2014)

No.	Sectors	No. of projects	Registered capital (million USD)	Share in total (%)
1	Manufacturing	9,600	141,406.7	56.0
2	Real estate	453	48,279.8	19.1
3	Construction	1,166	11,400.4	4.5
4	Accommodations & Food service	371	11,193.6	4.4
5	Production of electric devices, air conditioner	98	9,774.8	3.9
6	Information & Communication	1,095	4,124.9	1.6
7	Wholesale, retail & repair	1,383	4,030.7	1.6
8	Transportation & storage	448	3,755.3	1.5
9	Agriculture, forestry & fishing	528	3,721.8	1.5
10	Art, Entertainment & Recreation	148	3,634.2	1.4
11	Mining	87	3,375.3	1.3
12	Professional & scientific activities	1,698	1,797.4	0.7
13	Healthcare & medical service	97	1,754.6	0.7
14	Water supply, sewerage & waste management	38	1,348.5	0.5
15	Banking, finance & insurance	82	1,332.4	0.5
16	Education and training	204	819.9	0.3
17	Other services	141	754.1	0.3
18	Administration & support service	131	211.6	0.1
	Total	**14,942**	**252,716.0**	**100.0**

Source: Foreign Investment Agency.

Structure of FDI by partners

Regarding FDI partners, until 2014 Republic of Korea (ROK) had remained the biggest foreign direct investors of Vietnam among more than 100 countries and territories. The capital from ROK had added up to 37.7 billion USD (accounts for 15% of total FDI so far), following by Japan, Singapore, Taiwan (China), British Virgin Islands, Hong Kong (China), USA, Malaysia, China and Thailand. These countries make the top-ten biggest investors for Vietnam.

Republic of Korea, Japan, Singapore, and Taiwan (China) have always been the major investors for Vietnam since 25 years ago when the country started receiving FDI. One noteworthy point is that the increase of Japanese FDI in Vietnam in the last couple of years represents the strategic shift of investment of Japan towards “China+1” direction, due to the tension between Japan and China, as well as the hardship at the domestic market caused by the devastating tsunami in 2011. During the last few years, ROK and Taiwan (China) have also made several big investment projects in Vietnam, such as two Samsung mobile-phone manufactures in Bac Ninh and Thai Nguyen, with total capital amounts to 3 billion USD. Meanwhile, Taiwan (China) also has a large-scale steel production project of Formosa Corporation at Vung Ang, Ha Tinh with total capital exceeding 7 billion UDS. Singapore has a series of VSIP industrial parks that have attracted a large number of Singaporean investors into Vietnam.

Tax-havens, e.g. British Virgin Islands, Cayman and Samoa, are places where a huge number of transnational corporation (TNCs) registers their legal entity at in order to take full advantage of the low-rate tax system. Many of such TNCs also invest in Vietnam.

Table 3

Top 20 FDI investors in Vietnam (accumulated till 31/12/2014)

No	Investors	No. of projects	Registered capital (million USD)	Share in total (%)
1	Republic of Korea	4,190	37,726.3	15.0
2	Japan	2,531	37,334.5	14.8
3	Singapore	1,367	32,936.9	13.1
4	Taiwan, China	2,387	28,468.5	11.3
5	British Virgin Islands	551	17,990.0	7.2
6	Hong Kong	883	15,603.0	6.2
7	USA	725	10,990.2	4.4
8	Malaysia	489	10,804.7	4.3
9	China	1,102	7,983.9	3.2
10	Thailand	379	6,749.2	2.7
11	Netherlands	229	6,625.4	2.6
12	Cayman Islands	57	5,948.5	2.4
13	Canada	143	4,995.2	2.0
14	Samoa	122	4,270.2	1.7
15	France	426	3,324.5	1.3
16	United Kingdom	199	3,159.0	1.3
17	Russia	106	1,957.4	0.8
18	Switzerland	101	1,943.8	0.8
19	Australia	326	1,656.0	0.7
20	Brunei	160	1,624.4	0.6

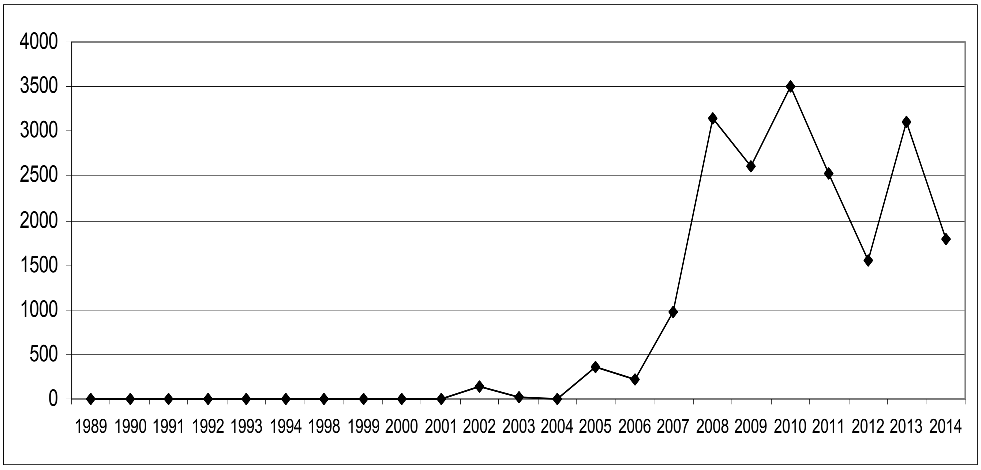
Source: Foreign Investment Agency

5. The outward direct investment of Vietnam

In 1989, Vietnam started investing in foreign country with a project worth 0.6 million USD. Until 31 December 2014, there have been 930 outward investment projects with total registered capital of 19.78 billion USD.

Figure 7

Vietnam outward direct investment, 1989-2014 (mln USD)



Source: Vietnam General Statistics Office.

Looking at 25-year-long history, one could see that the pre-2005 value of outward investment of Vietnam was trivial. Since 2005 (2 years before Vietnam accession to WTO), the value of outward FDI has increased significantly and reached the peak in 2010 when the value amounted to 3.5 billion USD.

In 2014, although the economy went through severe hardship, the outward FDI still managed to reach a satisfactory level. 109 investment projects were made in 28 countries and territories with total value of above 1 billion USD. 22 projects were adjusted and increased by 739 million USD. In terms of quantity, a large number of projects were directed into Cambodia (23 projects – 21% of the total), the rest includes Myanmar (16 projects – 14.7%); Laos (13 projects – 12%), USA (12 projects – 11%) and Singapore (9 projects – 8.2%). In terms of newly increased capital, a majority went to Tanzania (1 project – 34% of total registered capital), followed by Cambodia (31.1% of total registered capital), the third one is Burundi (2 projects – 16.2% of total registered capital). In terms of industrial sector, the capital was focused mainly on information and communication (54.3%); agriculture, forestry and fishery (27.5%); mining (6%). Some big projects with total capital exceeding 50 million USD have been made, e.g. Viettel's investment of telecommunication network in Tanzania, Burundi; investment for growing rubbery trees in Cambodia of An Dong Mia Company, Tay Ninh Rubber Company, Dau Tieng – Kratie Company, Tan Bien – Kampongthom Company.

It is easy to see that large-scale investment projects of Vietnam were primarily made in the telecommunication and agriculture-forestry-fishery industries. The destination countries include Lao PDR, Cambodia and several African nations. These fields and countries represents the preference of Vietnam's outward FDI. Recently, the country's new investment have been directed towards emerging economies, where economic potential is boutiful.

Regarding the implementation of direct investment in foreign countries, until 2014 accumulated implemented capital of Vietnam amounted to 6 billion USD, accounting for more than 30.6% total registered outward FDI. In which, oil industry had the highest level of implemented capital – 2.9 billion USD; the agriculture-forestry spent 660 million USD; hydro-power spent about 500 million USD; information and communication spent 450.6 million USD; banking, finance and insurance spent above 230 million USD…

Among total implemented capital of Vietnam's outward FDI, a large part was spent domestically (not transferred abroad). According to the report of Petrovietnam Corporation, Song Da Corporation, Vietnam Rubber Group, Vietnam national coal - mineral corporation, Viettel, etc., a part of outward FDI was paid to Vietnamese contractors or to purchase Vietnamese goods/service.

FDI in 2014 increased steadily. The number of projects increased by 10% compared with that of previous year. However, total registered capital decreased by 10% since most of them are of small-scale and focused primarily on trade and services. A major part of all investments were implemented in Cambodia and Myanmar and focus mainly on the fields of telecommunication and growing industrial trees, which are in line with the government's preferred direction.

The rest of total projects were scattered into different countries and territories, including ASEAN, Russia, Japan, ROK, EU, USA, Australia, Africa; focused mainly on trade and service sectors that Vietnamese enterprises were specialized in. Besides, other fields of investment include construction, transportation, real estate, manufacturing... This reflects the heterogeneity of Vietnam's outward FDI, and shows that seeking for new market is a modern trend of Vietnamese enterprises. The current strategy for Vietnamese firms is focusing on the fields that require less investment, turnover the capital more rapidly, and promote higher efficiency for enterprises. (Foreign Investment Agency, 2015).

6. Policy direction for a coming period

For restructuring the economy towards increasing quality of growth, and integrating more deeply into international and regional level – starting with AEC at the end of 2015 and new waves of FTA (TPP, EVFTA, Vietnam – EU), Vietnam should adjust her economic integration policy towards the following directions:

In trade, increase the processing and the added value of exported goods. Promote supporting industries in order to reduce import of input, increase the domestically-made part of goods that is made in Vietnam (to satisfy the rules-of-origin of FTAs). Improve the trade deficit that has been existing for a long time.

In attracting FDI, Vietnam should give priority to the following fields: high-tech, mechanical technology, information and communication, pharmacy, biology and renewable energy, clean energy, new materials, etc. Attract more FDI into infrastructure and supporting industries (in addition to traditional FDI, the country should also enhance PPP corporation). Restrict FDI in low-tech and polluted fields. Formulate policy that gives preferential treatment to large-scale investment projects that have positive spill-over effect to the whole economy.

Regarding Vietnam's outward FDI, the Government should continue building and completing sub-laws regulations that regulate outward FDI and outward FDI management models. These sub-laws facilitate and act as a guideline for individual's and enterprise's outward investment. They also serve as platform for state management in the field of outward FDI. The measures to promote and support FDI should be specifically synchronised and clearly defined, in which emphasis will be placed on providing information about investment environment and opportunities at destination country, protecting the rights of outward FDI enterprise when they operate abroad. The Government should also conduct activities and events to encourage domestic firms to invest and operate in foreign countries, keeping the tradition and seeking for potentially beneficial markets.

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