

MPRA

Munich Personal RePEc Archive

Has the U.S.-Vietnam Bilateral Trade Agreement Led to Higher FDI into Vietnam?

Parker, Steve; Phan, Vinh Quang and Nguyen, Ngoc Anh
DEVELOPMENT AND POLICIES RESEARCH CENTER

2005

Online at <http://mpra.ub.uni-muenchen.de/1384/>

MPRA Paper No. 1384, posted 07. November 2007 / 01:43

Has the U.S.-Vietnam Bilateral Trade Agreement Led to Higher FDI into Vietnam?

Steve Parker*, Phan Vinh Quang*, and Nguyen Ngoc Anh**

USAID-Funded STAR-Vietnam Project* and Ministry of Trade of Vietnam**1

Abstract In December 2001, a Bilateral Trade Agreement (BTA) came into effect that normalized economic relations between the United States and Vietnam. The resulting surge in trade surpassed most expectations. The impact of the BTA on FDI, however, has been less visible, especially with regard to U.S. FDI into Vietnam. This paper uses new data that accounts for FDI by U.S. subsidiaries resident in third countries to show that U.S. firms have been much more aggressive investors in Vietnam than normally reported in typical bilateral FDI data using Balance of Payments definitions of capital flows. While the U.S. is widely reported as the 11th largest investor into Vietnam, the new data shows that U.S.-related FDI exceeded all other countries in 2004. Although a formal model is not developed, descriptive data supports strongly the conclusion that the BTA has had a major impact on FDI into Vietnam, especially with regard to FDI from U.S. multinationals.

Keyword: FDI, Trade Agreement

JEL Classifications: F1

Introduction and Summary of Key Findings

The United States and Vietnam normalized economic relations with the coming into effect of the U.S.-Vietnam Bilateral Trade Agreement (BTA) on December 10, 2001.² The BTA is a comprehensive trade agreement based in large part on WTO Agreements, with extensive obligations regarding trade in goods and services, the protection of intellectual property rights (IPR), the development of investment, business facilitation, and transparency and the right to appeal.³ On the day that the BTA came into effect, the U.S. extended normal trade relations (NTR) status to Vietnam.⁴ This reduced tariff levels for imports from Vietnam into the United States from an average of around 40 percent to an average of around 4 percent, effectively removing prohibitively high tariff rates in most sectors and opening up the U.S. market for Vietnamese exporters. Although many in Vietnam were pessimistic about the ability of Vietnamese firms to compete in the U.S. market, the response was striking. Vietnamese exports grew five-fold from 2001 to the end of 2004, just three years after the BTA came into effect.⁵

Vietnam was required to meet the same extensive BTA obligations as the United States. As a transition economy not yet in the WTO, this required major changes in laws, regulations and administrative procedures, as well as improving market access for goods and particularly services for U.S. firms. The BTA, as a bilateral (not a free) trade agreement, required that

Vietnam reduce tariff levels on an MFN basis only on around 250 products, primarily in the agricultural sector.⁶ The BTA does, however, have strong requirements to improve the business environment for U.S. firms in Vietnam in general, including extensive obligations to improve the foreign investment climate for U.S. firms in Vietnam, particularly in service sectors. Recognizing Vietnam's developing country status and the role of the BTA as a "stepping stone" to WTO accession, Vietnam was allowed to phase in a number of important commitments over periods from two to ten years, particularly those related to market access for goods and services, investment performance, customs procedures and IPR protection. Nevertheless, U.S. exports to Vietnam doubled over the first three years of BTA implementation, in large part as a result of a major purchase of Boeing 777 aircraft by Vietnam Airlines, which was concluded just after the BTA came into force.

While the bilateral trade response to the BTA exceeded the expectations of many, the response of foreign direct investment (FDI) to the BTA, particularly U.S. FDI, was less apparent.⁷ Normally "reported" registered FDI flows from all countries using standard Balance of Payments definitions grew from US\$2.6 billion in 2000 to US\$4.2 billion in 2004, a solid 61 percent increase (see Figure 1). Reported implemented FDI, however, grew by just 18 percent over this period, coming to US\$2.85 billion in 2004. Normally reported U.S. FDI data provide an even less conclusive picture. Reported U.S. registered FDI almost doubled from 2000 to 2002, but then fell substantially in 2003 and 2004 to just US\$47 million. On the other hand, reported U.S. implemented FDI grew from US\$62 million to US\$162 million from 2000 to 2004, with strong increases in 2003 and 2004.⁸ In addition to the relatively erratic growth path following the implementation of the BTA, the levels of reported U.S. FDI remained quite small relative to overall FDI inflows. As commonly reported in Vietnamese publications, U.S. FDI levels accumulated from 1988 to 2004 ranked the U.S. as the 11th largest investor in Vietnam, obviously much smaller than would be expected from the largest economy in the world.⁹

This article uses new data developed by Vietnam's Foreign Investment Agency (FIA) in the Ministry of Planning and Investment (MPI) to review more carefully how FDI responded to the BTA. The new data present a much clearer and more positive picture of how FDI responded to the BTA, particularly with regard to U.S. FDI. "U.S.-related" FDI is calculated by adding FDI from U.S. overseas subsidiaries resident in third countries (like Singapore) to FDI sourced directly from U.S.-based firms. U.S.-related FDI grew dramatically in 2003 and 2004, surpassing FDI levels over this period from Japan, Korea, Taiwan and Singapore, traditionally the countries considered to be the largest investors into Vietnam.¹⁰ The new data provide a more robust empirical representation of how U.S. multinational firms manage their FDI into Vietnam. It shows clearly the problem with using typical bilateral Balance of Payments measures of FDI to analyze how multinational firms adjust their FDI decisions in response to major policy changes, especially in developing countries and especially for U.S.-based multinationals operating under U.S. tax laws. Based on this new data, it becomes clear that U.S. firms responded substantially more strongly than previously reported to the reforms induced by the BTA. Without the expansion of U.S.-related investment from 2000 to 2004, in fact, overall implemented FDI into Vietnam over that period would have grown by just 4 percent instead of the 18 percent actually recorded.

Two additional findings of note are reported. FDI to Vietnam by U.S. firms has been much higher than commonly reported for many years, with the new data showing that U.S.-related FDI accumulated from 1988 to 2004 is around three and one-half times higher than normally "reported" bilateral U.S. FDI. This is in line with the "visual" evidence of the existence

of many U.S. firms operating in Vietnam. As well, not only has U.S.-related FDI responded strongly to the BTA, there is also evidence that FDI from East Asian economies expanded substantially from 2000 to 2004 in those sectors where exports increased the most with the opening up of the U.S. market – that is apparel, footwear and furniture. This further reinforces the conclusion that the BTA has had a major positive impact on FDI flows into Vietnam.

The U.S.-Vietnam Bilateral Trade Agreement and Its Effects on the Environment for FDI To Vietnam

Investment Commitments under the U.S.-Vietnam Bilateral Agreement. The BTA is the most comprehensive trade agreement ever entered into by Vietnam. Investment is a key part of the BTA. The scope of investment covered by the BTA is not limited to direct investment but also includes indirect investment, including equity, bonds and other tangible and intangible assets. As an Agreement modeled on a WTO framework, the BTA includes all WTO commitments related to investment, including:

- Eliminating trade-related investment measures (WTO-TRIMs);
- Opening up goods and particularly service sectors for foreign investment under a schedule;¹¹
- Non-discrimination and elimination of dual price systems; and
- Transparency in the promulgation and implementation of investment policies.

As well, the BTA contains other provisions that go beyond the WTO Agreements related to investment and that are similar to those in typical investment protection agreements, such as the Vietnam-Japan Agreement on the Protection and Encouragement of Investment that was concluded two years after the BTA. Important commitments in the BTA that are not covered in the WTO include:

- Eliminating export performance requirements (which are not covered by TRIMs);
- Allowing licensing by registration for those foreign-invested projects not specified as sensitive sectors;
- Removal of restrictions on: i) equity participation; ii) the consensus principle for corporate governance in joint ventures; and, iii) some other limitations on the establishment and management of U.S.-invested enterprises;
- Allowing U.S. investors to set up joint stock companies and to issue securities in Vietnam; and,
- Provision of improved investment protection procedures and dispute settlement mechanisms between investors and the State, including access to international arbitration under the World Bank's International Center for Settlement of Investment Disputes (ICSID).

Some of the investment commitments in the BTA mentioned above were required to be applied over the first three years of BTA implementation, while a number of others are to be phased in over subsequent years.

A Review of How BTA Investment Commitments Have Been Implemented. Vietnam has implemented a number of important commitments in the BTA, and is scheduled to revise thoroughly by the end of 2005 its overall legal framework for investment and enterprise registration by developing a new Common Investment Law (CIL) and a new Unified Enterprise Law (UEL).¹² The CIL and UEL are expected to harmonize foreign and domestic investment and enterprise registration regimes, and are expected to liberalize access by foreign investors to a number of sectors, particularly service sectors. The exact market access reforms will be determined by the final resolution of the WTO accession negotiations, and will be applied on an MFN basis to all WTO members. The following is a brief review of the progress that has been made on implementing investment commitments in the BTA:

- **National Treatment (NT) and Most Favored Nation (MFN):** The Ordinance on MFN and NT provides a general legal framework for extending NT and MFN to foreign investors and traders. The CIL and UEL are expected to deal specifically with key NT issues related to investment.
- **Removal of Dual Pricing:** As of January 1, 2005, with adjustments for electricity, Vietnam completed its obligation to remove all dual pricing for services provided to foreign businesses.¹³
- **Removal of the Limitation on Technology Transfer:** Decree 27/2003/NĐ-CP removed the requirement that foreign contribution in the form of technology must be less than 20 percent of equity.
- **Mortgage of Land Use Rights:** The Foreign Investment Law and the new Land Law allow foreign investors to mortgage land use rights at credit institutions licensed to operate in Vietnam.
- **Eliminating TRIMs:**
 - The foreign-exchange-balancing requirement has been abolished under the Foreign Investment Law and Decision 46/2003/QĐ-TTg, which states that enterprises do not have to sell foreign exchange to banks by reducing the foreign exchange forced surrender rate to zero percent;
 - Vietnam does not apply import and export balancing requirements;
 - The Foreign Investment Law encourages but does not force companies to buy domestic products per local content requirements. However, in some sectors, taxes and various incentives may be based on how much local content is used in the production of a product; and,
 - Decree 27/2003/NĐ-CP removed the requirement that a certain level of exports is required to maintain a foreign investment license in some domestic industries, but other remains.
- **Market Access Commitments:** Recently, licensing authorities state that they have been applying the BTA to U.S. investors on a case-by-case basis. In a number of sectors, however, these rights for U.S. investors are not yet clearly provided for in written regulations published in the Official Gazette, as is required by the BTA.
- **Investment Dispute Resolution Commitment:** MPI has submitted to the Prime Minister a proposal to accede to the Washington Convention 1965 Resolution on disputes between a state and citizen of another country. MPI is working with other agencies to complete necessary legal procedures for submitting this Resolution to the President for final approval.

The Common Investment Law and the Uniform Enterprise Law are expected to meet a number of additional BTA commitments, including:

- Extension of licensing by registration to all sectors, except those with restrictions in the BTA/WTO;
- Liberalizing access by foreign investors in sectors per international commitments, including those scheduled under the BTA and the WTO accession protocol;
- Removal of restrictions on foreign investment, such as the minimum capital requirement, limits on the establishment of joint-stock companies, consensus decision making requirements, and the first refusal right to Vietnamese joint-venture partners; and,
- Full elimination of investment performance requirements in line with the TRIMs Agreement, which is essentially incorporated by reference in the BTA, and for export performance requirements as required by the BTA.

In addition to commitments directly affecting investment, Vietnam has made significant progress toward implementing other commitments in the BTA that help improve the business environment for both domestic and foreign firms. These include improving transparency by requiring publication of regulations before their effectiveness, reforming court procedures to make the courts more independent and effective, improving the arbitration process, modernizing contract law, reforming legal and banking service sectors, and implementing customs valuation based on transaction value. Although major improvements are being made in the business environment for FDI in Vietnam, important constraints remain.¹⁴

The Expected Impact of the BTA on Overall and U.S. FDI in Vietnam. When analyzing the impact of the BTA on FDI, it is important to take into account the relative competitive advantages of firms in Vietnam, the United States and third countries. The competitive advantage of U.S. companies typically focus on more capital/skill/technology-intensive sectors, such as financial, legal, telecommunications and distribution services, information technology and chemical manufacturers, and oil and gas and other capital-intensive, natural-resource-based production. U.S. firms are typically strong in sectors where intellectual property is important. Vietnam's comparative advantage for exports, on the other hand, tends toward labor-intensive sectors such as clothing, furniture and footwear, and natural-resource-intensive sectors such as tropical agricultural production, oil and gas, and mining. While U.S. buyers have an aggressive presence in Vietnam, it is relatively rare for U.S. firms to invest in labor-intensive export production.¹⁵ For these sectors, FDI from Vietnam's East Asian neighbors is much more typical. As such, this analysis would predict that the opening of the U.S. market for labor-intensive exports from Vietnam would increase FDI primarily from regional Asian investors rather than from the United States. Over time, however, Vietnamese exports should diversify into sectors where U.S. firms have stronger competitive advantages, and thus it should be expected that export-related U.S. FDI should expand over time.

Firms also will invest in Vietnam because of opportunities to export to countries other than the United States. To the degree that the BTA improves the business environment in Vietnam, such FDI should increase as well. Probably most importantly, however, opportunities in the domestic economy are increasingly attractive for foreign investors. In this regard, the BTA represents one part of a much broader effort by the Vietnamese government to develop its

economy and to improve its business environment. Vietnam's economy has grown by an annual average of around 7 percent over the last decade, is beginning to industrialize quickly, and has a relatively well-educated population of around 82 million with relatively broad-based increases in standards of living and steady declines in poverty levels. These strong economic fundamentals, combined with widely perceived political stability, create demand for FDI into Vietnam for building all types of physical and social infrastructure, for building industry and developing services to meet rising consumer demand and to support the industrialization process, and for extracting major reserves of natural resources, especially oil and gas.

Overall FDI Flows into Vietnam and the Impact of the BTA

As shown in Figure 1, after the spike in the mid-1990s, FDI into Vietnam increased moderately from 1999 to 2004. Although growth in registered FDI picked up a bit from 2001 to 2004 as the BTA was being approved and implemented, most likely representing some increased interest in overall FDI related to the BTA, FDI actually implemented has grown quite modestly since 1997. Furthermore, many other reforms not directly related to the BTA have been enacted from 2000 to 2004, making it difficult to discern the direct impact of the BTA on FDI.

FDI into Vietnam depends not only on Vietnamese policies, but also on the policies of other countries competing for similar FDI and on factors affecting foreign investors, both of which are beyond the control of Vietnam. Table 1 shows that global and regional FDI flows have experienced a sharp decline since 2000. Despite the vibrant economies in Southeast Asia and China, FDI inflows into East and Southeast Asia dropped by more than a third from US\$143 billion in 2000 to US\$97 billion in 2003. The global FDI picture was even bleaker, with a sharp decline by more than one-half, from US\$1,388 billion in 2000 to US\$560 billion in 2003.¹⁶ Furthermore, FDI to China continued to grow solidly in this period, partly as a result of China's accession to the WTO in 2001, increasing from US\$41 billion in 2000 to US\$53 billion in 2003. This increase in FDI to China means that FDI to other Southeast and East Asian economies fell even more severely than the regional numbers would imply. If we assess Vietnam's FDI performance against this background, Vietnam actually fared well in relative terms compared to most of its regional neighbors. Other than China, Vietnam was one of the few countries in the world where FDI increased from 2000 to 2003. This suggests that Vietnam's reforms appear to have had a more positive impact on FDI than is commonly perceived when country-level results are reviewed in isolation. On the other hand, Vietnam did not keep up with China's path-breaking success in attracting FDI over this period.

An interesting feature of FDI into Vietnam since the mid-1990s peak is that the number of registered FDI projects has increased while the average size of a FDI project has declined (see Figure 2).¹⁷ From 1996 to 2002, FDI into Vietnam was made increasingly in the form of smaller projects, rather than the larger projects registered in the mid-1990s. This trend changes after the coming into force of the BTA, with the average size of new registered projects increasing in size somewhat after 2001. From 2002 to 2004, nevertheless, the average FDI project represented a relatively small capital investment and was made increasingly in light manufacturing industries (as reported by the FIA). This feature is not necessarily good or bad. For a country with a comparative advantage in labor-intensive exports, one would expect smaller capital investments. On the other hand, this trend clearly shows that there has not been many large, new FDI projects in infrastructure and heavier industry.

In order to explore more directly the implications of the BTA on FDI, we examine FDI flows in clothing, furniture and fisheries, three sectors that have experienced strong export growth to the U.S. since the entry into force of the BTA. As shown in Table 2, registered FDI in these three sectors clearly started to pick up in 2000, the year that the BTA was signed, and have continued to post solid results over the last four years.¹⁸ According to the FIA and company interviews, many of these projects were aimed at exporting to the United States and originated from other East Asian countries. Ninety-three percent of FDI in the clothing sector from 2000 to 2004, for example, originated from investors in Asia, mostly from Taiwan, Hong Kong, Korea and Singapore. Reported U.S. FDI accounted for only 1 percent of total FDI in the apparel sector.

The important contribution of FDI into these three sectors targeted toward export opportunities to the U.S. opened up by the BTA was substantial during this period.¹⁹ As shown in Table 2, the share of the three sectors in total registered capital increased from a mere 3 percent in 1998 to 25 percent in 2001, and then leveled off to around 16 percent in 2003 and 2004. In absolute terms, registered FDI in these sectors increased from around US\$130 million in 1998 and 1999 to a peak of US\$804 million in 2001. FDI in these sectors remained strong from 2002 to 2004, reaching US\$670 million in 2004. Clearly, without the major expansion of FDI in these BTA-related-export sectors, Vietnam's overall FDI performance would have been substantially weaker over the last five years.

FDI in clothing appears to have been affected by the imposition of quotas by the U.S. on Vietnamese-based clothing exporters in 2003, as represented by a slight decrease in FDI in 2003.²⁰ However, FDI in clothing rebounded quickly in 2004. According to interviews with garment companies, three reasons were given to explain the strong expansion of FDI in the clothing sector in 2004. First, clothing producers expect to take advantage of the elimination of the U.S. quota when Vietnam accedes to WTO, which they apparently expect to happen in the near future. In this regard, they are investing their funds because they expect that Vietnam will be able to compete effectively with China and others in the global clothing market. Second, some companies have been able to expand the export of quota-free items to the United States. And, third, the elimination of the EU quota on Vietnamese clothing exports opened up new market opportunities. With the positive attitude by foreign investors that Vietnam can compete in an unregulated global market for apparel, reinforced by recent policies to limit imports of apparel products from China into the U.S. and EU markets, it is expected that FDI in the Vietnamese clothing sector will remain strong, especially if Vietnam accedes to the WTO by the end of 2005 as currently targeted and can then benefit from the elimination of U.S. textile quotas.

In line with the registered data, implemented FDI in the clothing sector recorded a solid, steady increase from US\$84 million in 1998 to US\$204 million in 2004 (see Table 3). Growth picked up somewhat from 2001 to 2004, the years of BTA implementation. Comparing 1998 to 2004, the share of FDI in clothing to total implemented FDI doubled from 3.5 percent to 7.2 percent. Although this Report focuses on FDI, the opening of the U.S. market and BTA-related improvements in the business and investment environment almost surely have also stimulated domestic investment, including in the clothing sector where a number of Vietnamese firms (often state-owned firms) expanded capacity quickly to meet the surge in demand for exports of clothing to the United States following the coming into effect of the BTA.

U.S. FDI into Vietnam and the Impact of the BTA

“Reported” U.S. FDI to Vietnam. According to the official statistics normally reported by MPI, from 1988 through December 31, 2004, “reported” registered U.S. FDI into Vietnam amounted to US\$1.3 billion, of which US\$730 million had been implemented in 215 projects in manufacturing, oil and gas, agriculture and services sectors (see Table 3). The U.S. ranked 11th among 75 investing countries into Vietnam at the end of 2004.²¹

As shown in Figure 3, reported registered U.S. FDI to Vietnam has trended steadily downward since the “boom” period in the mid-1990s. After a bump up in 2001 and 2002 during the period when the BTA was coming into effect, registered U.S. FDI actually fell substantially in 2003 and 2004, even as a number of BTA commitments were set to be phased in. This data would clearly lead to the presumption that the BTA has not had a major effect on U.S. FDI to Vietnam. Implemented U.S. FDI data, however, presents a more positive result, growing solidly in 2003 and 2004. Even with this growth, however, reported implemented U.S. FDI remained much smaller than FDI from many other countries after the BTA (see Figure 3 and Table 6).

U.S.-Related FDI to Vietnam. In order to assess the full response of U.S. investors to the BTA, it is necessary to consider not only FDI sourced directly from the U.S., but also to examine FDI made by U.S. overseas subsidiaries resident in third countries. For a number of reasons, we expect that U.S. firms will invest in Vietnam strongly through their overseas subsidiaries, especially their Asian regional headquarters. First, the BTA covers not only investment sourced in the U.S., but it also covers on an equal basis investment made by U.S. subsidiaries resident in third countries. Second, and quite importantly, based on interviews with a number of U.S. firms operating in Vietnam, many noted that U.S. tax laws encourage U.S. firms to source their investment from overseas subsidiaries. Third, there can be managerial and other business operation benefits to having an investment in Vietnam managed by a close-by regional headquarters, especially since most U.S.-related FDI projects in Vietnam tend to be relatively small. MPI reports that a number of prominent U.S. firms operating in Vietnam have sourced their FDI from third countries.²² For example, American Home, Coca Cola, Proctor and Gamble, Caltex and American Standards are invested out of Singapore; Baker & McKenzie and Exxonmobil are sourced from U.S. subsidiaries in Hong Kong; Conoco is invested from the United Kingdom; and Pepsi, British American Tobacco, KPMG and Cisco are investments by U.S. subsidiaries in Holland. A large oil and gas investment by a U.S. firm originated from Mauritius. As a result, to assess carefully the response of U.S. firms to the impact of the BTA, it is necessary to analyze data that reports on FDI from overseas U.S. subsidiaries as well as FDI sourced directly from the United States.

To facilitate this research, based on reports from all major provinces in Vietnam, the FIA reviewed as many foreign-invested project reports as possible to determine whether the FDI was sourced directly from a U.S.-based firm or from a U.S. overseas subsidiary registered in a third country. A new type of FDI data has been calculated by MPI to capture more fully how U.S. multinationals manage their FDI decisions in Vietnam – “U.S.-related” FDI. U.S.-related FDI equals FDI reported as sourced from the U.S.-based firms (the typical FDI reported by MPI) plus FDI from overseas U.S. subsidiaries sourced from third countries. Given the limitations of this study, it is not possible to make similar adjustments to FDI from other countries. As a result, this Report cannot re-rank U.S.-related FDI relative to other countries “related” FDI.

In comparison to reported U.S.-based FDI, U.S.-related FDI provides a considerably different, and much more positive, picture regarding how U.S. investors have contributed to Vietnam's economy over the last seventeen years and have responded to the BTA over the last three years (see Figure 4 and Table 4). Looking first at cumulative FDI as most commonly reported by MPI, U.S.-related initial registered FDI from 1988 through 2004 was US\$2.602 billion compared to the reported initial registered U.S. FDI of US\$1.291 billion. The difference is even more profound for implemented FDI, with U.S.-related implemented FDI equaling \$2.634 billion compared to reported implemented U.S. FDI of US\$730 million. For the cumulative data, U.S.-related registered FDI is more than double the stock of reported registered U.S. FDI, and U.S.-related implemented FDI is more than three and a half times the stock of reported implemented U.S. FDI. Interestingly, as shown in Table 5, levels of U.S.-related FDI were considerable from 1996 through 2001, before the BTA and during a time when overall FDI to Vietnam was relatively weak. Clearly, the new data on U.S.-related FDI confirm that U.S. firms have been much more strongly invested in the Vietnamese economy over the last ten to fifteen years than the normal reported FDI has led one to believe.

U.S.-related investment increased significantly after the entry into force of the BTA, especially in the years 2003 and 2004 (see Figure 4 and Table 5). Over the pre-BTA period, from 1996 to 2001, the average growth of U.S.-related implemented FDI was minimal, just around 3 percent per year. From 2001 to 2004, however, U.S.-related implemented FDI surged by an average of 27 percent per year. U.S.-related FDI was particularly strong in 2003 and 2004, achieving levels around two times higher than normal years in the past. Furthermore, U.S.-related implemented FDI from 2002 to 2004 totaled to US\$1.149 billion, while regular reported implemented U.S. FDI came to just US\$355 million. In this regard, U.S.-related FDI was around three times higher than the regular reported U.S. FDI since the BTA came into effect. Furthermore, during this difficult global period for FDI (see Table 1), overall implemented FDI to Vietnam would have increased by just 4 percent from 2000 to 2004 without the robust expansion in U.S.-related FDI compared to the actual 18 percent growth achieved over this period. Clearly, U.S. investors have responded quite positively to the coming into force of the BTA, and the regular reported FDI data have strongly under-reported how U.S. firms have responded to the BTA.

Lastly, U.S.-related FDI to Vietnam has grown more strongly since the BTA than has non-U.S. FDI (see Figure 5 and Table 6). In 2003, U.S.-related FDI surged to the second largest level among all countries, just below Japan. In 2004, U.S.-related FDI exceeded all other countries. This result, in fact, qualifies the argument that the initial investment response to the BTA may be dominated by East Asian firms investing in Vietnam to export labor-intensive products to the newly opened U.S. market. Although it appears that East Asian FDI did increase in some key sectors related to exporting to the U.S. market (as noted above for clothing, furniture and fisheries), U.S.-related FDI also increased markedly as the BTA came into force and was implemented in large part successfully over time.

Around three-quarters of FDI originating from overseas U.S. subsidiaries has come from Singapore and one big oil and gas project from Mauritius (made before the BTA). Other countries serving as important bases for FDI from U.S.-subsidiaries include Holland, Hong Kong, British Virgin Islands and Bermuda (see Table 7). Since these data are available only on an accumulated basis from 1988 to 2004, it is not possible to determine from which resident third countries the substantial increase in FDI from overseas U.S. subsidiaries in 2003 and 2004 was sourced from. Based on lists of firms provided by the FIA, however, it appears that a substantial

proportion of such FDI was sourced from Singapore, and it is clear that it was not sourced from Japan, Taiwan or Korea.

Table 4 breaks down U.S.-related and reported U.S. FDI by economic sector. Cumulated from 1988 through 2004, U.S.-related implemented FDI totaled US\$2.633 billion, consisting of 267 projects employing 16,853 people by the end of 2004. In fact, 72 percent of U.S.-related implemented investment worth US\$1.9 billion was from overseas subsidiaries of U.S. companies, while only 28 percent has been funded directly from the United States. The majority of U.S.-related FDI is in heavy industry, food processing and oil and gas, which have accounted for 74 percent of accumulated U.S.-related implemented FDI.²³ The most common type of FDI has been in the form of 100-percent foreign ownership (72 percent of the number of U.S.-related projects), but this has accounted for only 42 percent of total U.S.-related implemented FDI. Joint ventures and business cooperation contracts (BCCs) accounted for 25 percent and 33 percent of total implemented U.S.-related FDI, respectively. The high percentage of U.S. FDI in the form of BCCs is due to several large projects in the oil and gas sector, which by regulation can only take the form of BCCs. Most U.S.-related investment is located in Ho Chi Minh City and Binh Duong, Dong Nai and Vung Tau provinces in the South, Ha Noi and the province of Hai Duong in the North, and in unspecified locations for oil and gas.²⁴

Conclusions and Suggestions for Further Research

This is the first study made on the impact of the BTA on FDI into Vietnam. New data collected by Vietnam's Ministry of Planning and Investment show clearly that the BTA has had a significant, positive impact on overall FDI, and particularly U.S.-related FDI, into Vietnam. These findings are based on descriptive analysis – no attempt is made to develop a more sophisticated economic model that could more carefully isolate the impact of the BTA relative to other factors affecting FDI into Vietnam. Another finding demanding more in-depth research is how the BTA affected domestic investment and private sector development. We hope that these descriptive results stimulate new questions and further research on FDI flows into Vietnam, and that it can serve as a benchmark for assessing the impact on FDI of Vietnam's pending WTO accession. To facilitate further research, the authors would be happy to provide more details on the data and survey results presented in this study.

References

1. Steve Parker and Phan Vinh Quang are Director and Deputy Director of the USAID-funded STAR-Vietnam Project, respectively. The STAR Project supports the State of Vietnam to implement the U.S.-Vietnam Bilateral Trade Agreement and to accede to the World Trade Organization. Nguyen Ngoc Anh is a Lecturer of Economics at the Hanoi Business School and Senior Expert at the American Department of Vietnam's Ministry of Trade. This article does not necessarily represent the views of the U.S. Agency for International Development, the STAR-Vietnam Project, or the Government of Vietnam.
2. This article draws heavily from a preliminary July 2005 Report prepared by Vietnam's Foreign Investment Agency in the Ministry of Planning and Investment and the STAR-Vietnam Project on "The Impact of the U.S.-Vietnam Bilateral Trade Agreement on Overall and U.S. Foreign Direct Investment in Vietnam (MPI/STAR Report)". The final report is

expected to be published by the end of September, 2005. This and the other reports referenced from STAR are available on the Vietnam Chamber of Commerce and Industry's "Vietnam Business Forum" webpage: <http://www.vibonline.com.vn/>.

3. The BTA is provided in full on the U.S. Trade Representative Website and is printed in Vietnam's Official Gazette.
4. NTR is equivalent to the more commonly used term Most Favored Nations (MFN) Treatment, which means that one country agrees to treat equally all other countries with NTR/MFN status. As a founding WTO member, with the extension of NTR/MFN treatment to Vietnam, the U.S. immediately complied with the obligations of the BTA.
5. For a more detailed description of the BTA and its initial implementation, its link to the WTO, and the subsequent bilateral trade response to the coming into effect of the BTA, see the 2002 Annual Report on "An Assessment of the Economic Impact of the U.S.-Vietnam Bilateral Trade Agreement," and the "Update on Bilateral Trade in 2003 Between Vietnam and the United States," both produced by the Vietnamese Central Institute of Economic Management (CIEM) and STAR.
6. To be clear, the BTA is a "bilateral-trade" agreement that normalized trade relations between the two countries, it is not a "free-trade" agreement. Extensive reductions in Vietnam's tariff levels are expected to be made on a MFN basis as a result of Vietnam's WTO accession negotiations, for which the Vietnamese Government has set a self-imposed deadline for accession by the end of 2005.
7. The MPI/STAR Report examines FDI only. It does not include other forms of foreign investment, such as portfolio investment in capital markets, and does not assess what should be the important impact of the BTA on domestic investment. In this regard, FDI would include such investment by overseas Vietnamese under the Foreign Investment Law but would exclude investment made by overseas Vietnamese that may be registered as domestic investment under the Domestic Investment Encouragement Law.
8. As is typical for most reporting on FDI throughout the world, MPI reports FDI based on standard Balance of Payments definitions, which designates the origin of FDI as the country where the funding of the investment originates. This importantly and accurately measures capital flows from one country to another, but, as noted, it does not adequately capture how many U.S. multinational companies manage their investment decisions.
9. See the weekly magazine "Vietnam Investment Review" published by the Ministry of Planning and Investment.
10. MPI was not able to determine FDI originating from non-U.S. overseas subsidiaries. As a result, it is not possible to do a re-ranking of "related" FDI for all countries.
11. The WTO accession agreement will most likely require a greater number of service sectors to be opened in a shorter time period than did the BTA commitments.

12. In recognition of the importance of the BTA to international integration and improving the business environment, the National Assembly of Vietnam issued Resolution No. 48/2001/QH10 dated November 28, 2001 instructing various government agencies to amend laws and regulations to implement the BTA.
13. Note that this applies only to foreign businesses. Foreign individuals still pay a higher price for electricity. Dual prices for other fees had been removed earlier, including for: water, phone installation, air transportation and advertising.
14. Results from a survey of 81 foreign firms conducted for the full MPI/STAR Report show that the BTA tended to have a positive effect on their investment decisions. This tendency was strongest for U.S. firms and for firms exporting to the United States. Regarding which parts of the BTA most importantly influence investment decisions, firms stressed the importance of improving transparency, removing discrimination between domestic and foreign firms, streamlining the investment licensing system, opening more sectors to FDI and improving IPR enforcement. U.S. firms stressed more than non-U.S. foreign firms the importance of removing discrimination, opening more sectors to FDI, improving IPR protection and improving dispute resolution. When all general considerations for improving the business and investment environment were taken into account, not just those emphasized by the BTA, the firms stressed the importance of enforcing laws evenly and effectively, of joining the WTO and of improving the tax and investment licensing systems. U.S. firms compared to non-U.S. foreign firms stressed the importance of agreements on tax, trade and investment. Although firms responding to the survey noted that the investment environment in Vietnam had clearly improved recently, importantly in part as a result of the BTA, they clearly stress the importance of continuing to develop a more transparent legal system with more effective, uniform and predictable enforcement of laws and policies. For additional perspectives by businesses in Vietnam, see the Vietnam Business Forum webpage: "www.vietnambusinessforum.org".
15. The case of NIKE's role in Vietnam is a good example of this situation. NIKE is one of, if not, the largest purchaser of Vietnamese products, but it actually does not own any factories in Vietnam. All NIKE products are produced on a contract basis. In 2001, NIKE purchased US\$450 million exports from Vietnam produced by 6 foreign-invested shoe makers and 20 garment factories. By 2004, NIKE had increased exports from Vietnam to US\$728 million purchased from 9 foreign-invested shoe makers and 30 garment factories. These firms in combination employed about 130,000 people in Vietnam. Vietnam is the second largest manufacturing base for NIKE athletic shoes, accounting for 22 percent of NIKE's total global volume. Clearly, NIKE has expanded strongly its purchases of goods from Vietnam since the coming into effect of the BTA. Also clearly, in this case, the BTA has stimulated greater FDI into Vietnam from regional investors such as Taiwan and Korea to produce products for NIKE, and has stimulated domestic investment in factories that enter into contract manufacturing relationships with the NIKE buyers (see the Vietnam Economic Times, May 18, 2005 and a column from the Dow Jones Newswire).
16. See the UNCTAD FDI database (www.unctad.org).

17. Registered new capital is used to examine new FDI projects, because implemented investment in a certain year can represent the cumulative impact of the implementation of a registered investment over time.
18. The technical negotiations for the BTA were concluded in 1999 and the BTA was signed by the two governments on July 13, 2000. It was passed by the U.S. Congress on October 3, 2001 and signed by the U.S. President on October 16, 2001. It was ratified by the Vietnamese National Assembly on November 28, 2001 and signed by the President of Vietnam on December 7, 2001. The BTA came into force on December 10, 2001.
19. Clothing exports to the U.S. grew from US\$48 million in 2001 to US\$2.6 billion in 2004 despite the introduction of the textile quota. Fisheries exports to the U.S. rose from US\$512 million in 2001 to US\$732 million in 2003 and then declined to US\$568 million in 2004 as a result of anti-dumping cases for catfish and shrimp. Furniture exports to the U.S. increased from US\$13 million in 2001 to US\$386 million in 2004. In this regard, Vietnam benefited from a U.S. anti-dumping suit against Chinese furniture producers. For a more comprehensive review of trade flows between Vietnam and the U.S., please refer to the Economic Reports of STAR-Vietnam posted on www.vibonline.com.vn.
20. The full text of the “Agreement Relating to Trade in Cotton, Wool, Man-Made Fiber, Non-Cotton Vegetable Fiber and Silk Blend Textiles and Textile Products between the Governments of the United States of America and the Socialist Republic of Vietnam” is available on the Department of Commerce website: “otexa.ita.doc.gov/#IMPORTQUOTAS”. The agreement was signed on July 17, 2003, and applied retroactively to May 1, 2003. The agreement set quantitative limits (not value limits) on exports of certain textile and apparel items, which altogether accounted for about 90 percent of textiles and apparel exported by Vietnam to the U.S. in early 2003. The working assumption in the agreement was that the export value allowed by quota in the base year of 2003 was approximately US\$1.7 billion. The agreement allowed for the quotas to be automatically extended to 2004 and beyond. It allows Vietnam in each year to “Swing” quota limits from one (not fully used) category into another (fully used) category by up to 6 percent, as long as a corresponding reduction is made. It also allows exporters each year to redistribute quota not used up in one category to a category that is full, and to “carryover” unused quota for a product from one year to the next, not to exceed 11 percent. The 2003 quotas could grow in 2004 and subsequent years by 7 percent for non-wool products and 2 percent for wool products. While the U.S. eliminated textile quotas for all WTO members in line with the Uruguay Round commitment to phase out fully the WTO’s Agreement on Textiles and Clothing by January 1, 2005, the U.S. is maintaining its quota on Vietnamese apparel imports until Vietnam accedes to the WTO.
21. See the weekly magazine “Vietnam Investment Review” published by the Ministry of Planning and Investment.
22. Many other FDI projects by major U.S. firms, of course, have been sourced directly from the United States. For example, major investments by Ford, Citibank, Kimberly Clark, Cargill, Colgate and Unocal are sourced from the United States. Although considerably more numerous in terms of the number of projects than those sourced from overseas subsidiaries,

FDI sourced directly from the U.S. tend to be smaller in value terms and are reported by the FIA to have a higher rate of failure than those sourced from overseas U.S. subsidiaries resident in third countries.

23. Data are currently not available to provide a more detailed sectoral breakdown of the heavy industry aggregate. Major FDI by Coca-Cola and Pepsi overseas subsidiaries are included in the food processing sector.
24. For detailed FDI data by province, see the forthcoming MPI/STAR Report on “The Impact of the U.S.-Vietnam Bilateral Trade Agreement on Overall and U.S. Foreign Direct Investment in Vietnam.”

References

Center Institute for Economic Management and STAR-Vietnam. 2003. “An Assessment of the Economic Impact of the United States-Vietnam Bilateral Trade Agreement: Annual Economic Report for 2002,” National Publishing House, June.

Center Institute for Economic Management and STAR-Vietnam. 2003. “An Assessment of the Economic Impact of the United States-Vietnam Bilateral Trade Agreement: Economic Report for the First Six Months of 2003”, National Publishing House, December.

Center Institute for Economic Management and STAR-Vietnam. 2004. “An Assessment of the Economic Impact of the United States-Vietnam Bilateral Trade Agreement: Trade Update Report for 2003,” National Publishing House, June.

Ministry of Planning and Investment’s Foreign Investment Agency and STAR-Vietnam. 2005. “The Impact of the U.S.-Vietnam Bilateral Trade Agreement on Overall and U.S. Foreign Direct Investment in Vietnam,” forthcoming in September.

Multilateral Investment Guarantee Agency. 2002. Foreign Direct Investment Survey, January.

Otexa.ita.doc.gov/#IMPORTQUOTAS.

United Nation Conference on Trade and Development. 2004. World Investment Report.

U.S.-Vietnam Trade Council. 2004. “The U.S-Vietnam Bilateral Trade Agreement: A Survey of U.S. Companies on Implementation Issues,” May 10.

Vietnam Business Forum On-Line. Vietnam Chamber of Commerce and Industry, www.vibonline.com.vn.

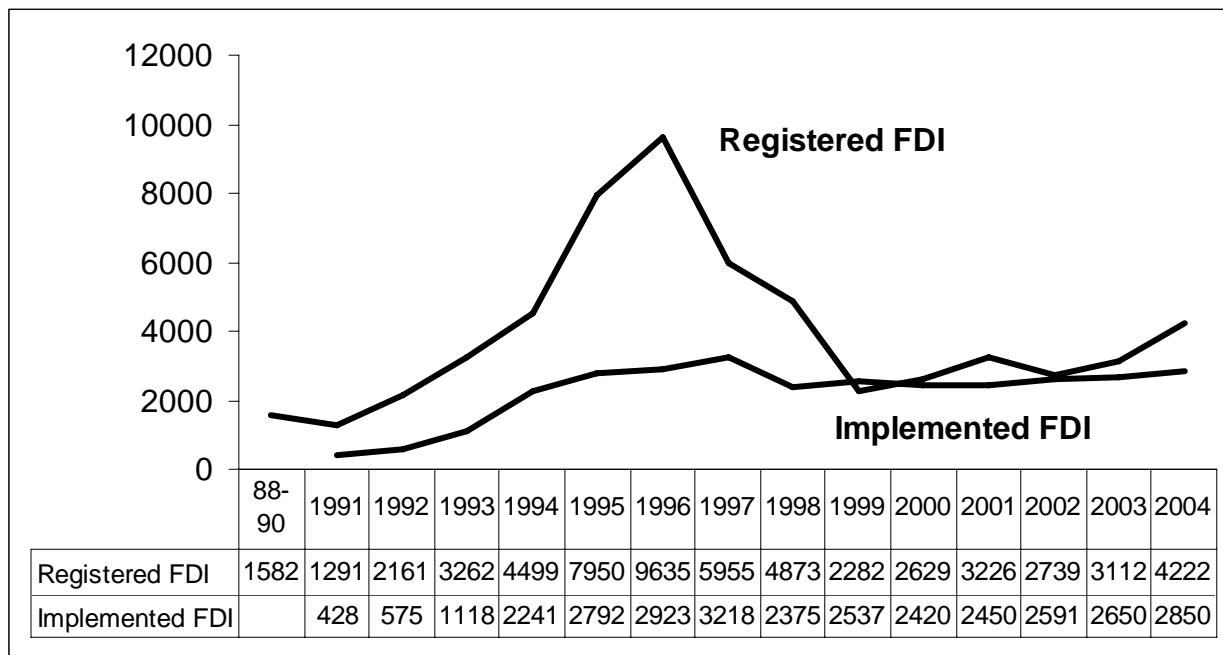
Vietnam Business Forum. International Finance Corporation, www.vietnambusinessforum.org.

Vietnam Economic Times. 2005. May 18.

Vietnam Investment Review. a weekly magazine published by the Ministry of Planning and Investment.

FIGURES AND TABLES:

Figure 1: Overall Registered and Implemented FDI from All Countries (US\$ millions)

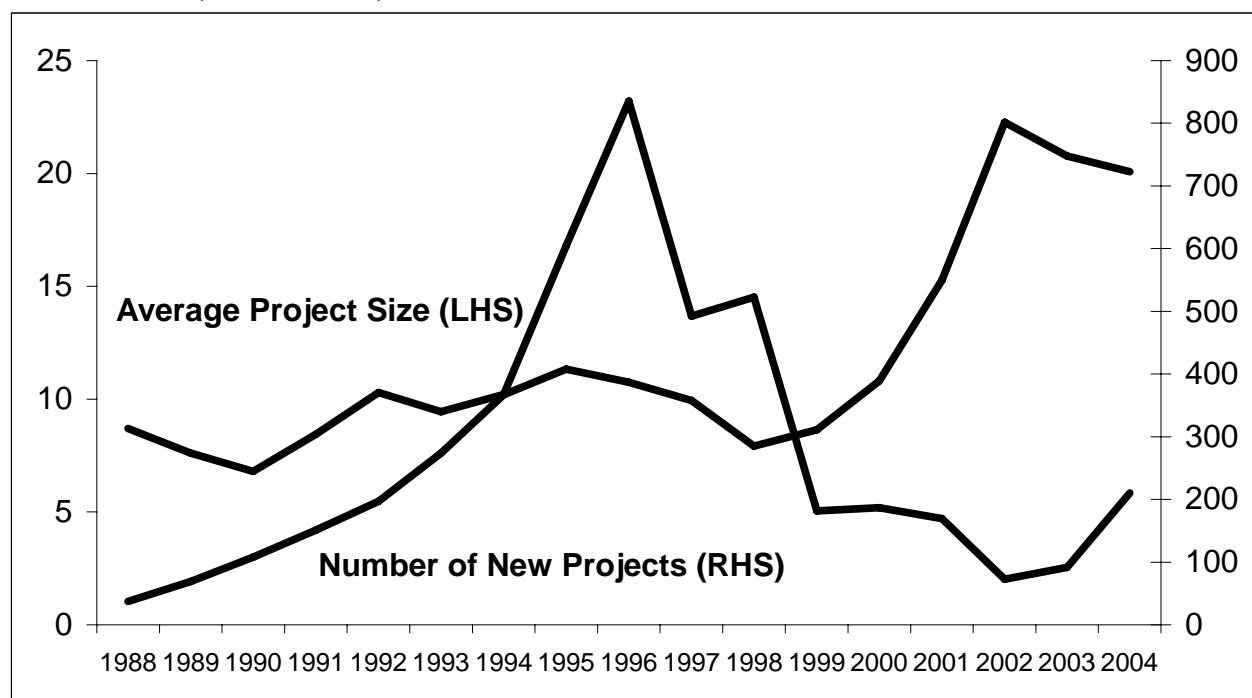


Source: MPI. The FDI data in this figure are not adjusted for dissolved and expired projects.

Table 1: FDI Inflows by Region (US\$ billions)

Region/country	FDI inflows						
	1992-1997 (Annual average)	1998	1999	2000	2001	2002	2003
Developed countries	180.8	472.5	828.4	1 108.0	571.5	489.9	366.6
Western Europe	100.8	263.0	500.0	697.4	368.8	380.2	310.2
European Union	95.8	249.9	479.4	671.4	357.4	374.0	295.2
Other Western Europe	5.0	13.1	20.7	26.0	11.4	6.2	15.1
Japan	1.2	3.2	12.7	8.3	6.2	9.2	6.3
United States	60.3	174.4	283.4	314.0	159.5	62.9	29.8
Developing economies	118.6	194.1	231.9	252.5	219.7	157.6	172.0
Africa	5.9	9.1	11.6	8.7	19.6	11.8	15.0
Latin America and the Caribbean	38.2	82.5	107.4	97.5	88.1	51.4	49.7
Asia and the Pacific	74.5	102.4	112.9	146.2	112.0	94.5	107.3
Asia	74.1	102.2	112.6	146.1	111.9	94.4	107.1
West Asia	2.9	7.1	1.0	1.5	6.1	3.6	4.1
Central Asia	1.6	3.0	2.5	1.9	3.5	4.5	6.1
South, East and South-East Asia	69.6	92.1	109.1	142.7	102.2	86.3	96.9
South Asia	2.5	3.5	3.1	3.1	4.0	4.5	6.1
The Pacific	0.4	0.2	0.3	0.1	0.1	0.1	0.2
Central and Eastern Europe	11.5	24.3	26.5	27.5	26.4	31.2	21.0
World	310.9	690.9	1 086.8	1 388.0	817.6	678.8	559.6

Source: UNCTAD, World Investment Report, 2004.

Figure 2: The Number and Average Size of New Registered FDI Projects in Vietnam (US\$ millions)

Source: MPI and the General Statistical Office.

Table 2: Share of Registered FDI in Clothing, Furniture and Fisheries to Overall Registered FDI from 1998 to 2004 (US\$ millions)

	1998	1999	2000	2001	2002	2003	2004
Clothing	60	54	122	657	349	337	420
Furniture	52	68	80	108	108	96	232
Fisheries	15	9	16	39	37	52	18
Total registered FDI of three sectors	127	131	218	804	494	485	670
Total registered FDI	4,781	2,197	2,485	3,224	2,757	3,064	4,200
Share of three sectors in overall registered FDI	3%	6%	9%	25%	18%	16%	16%

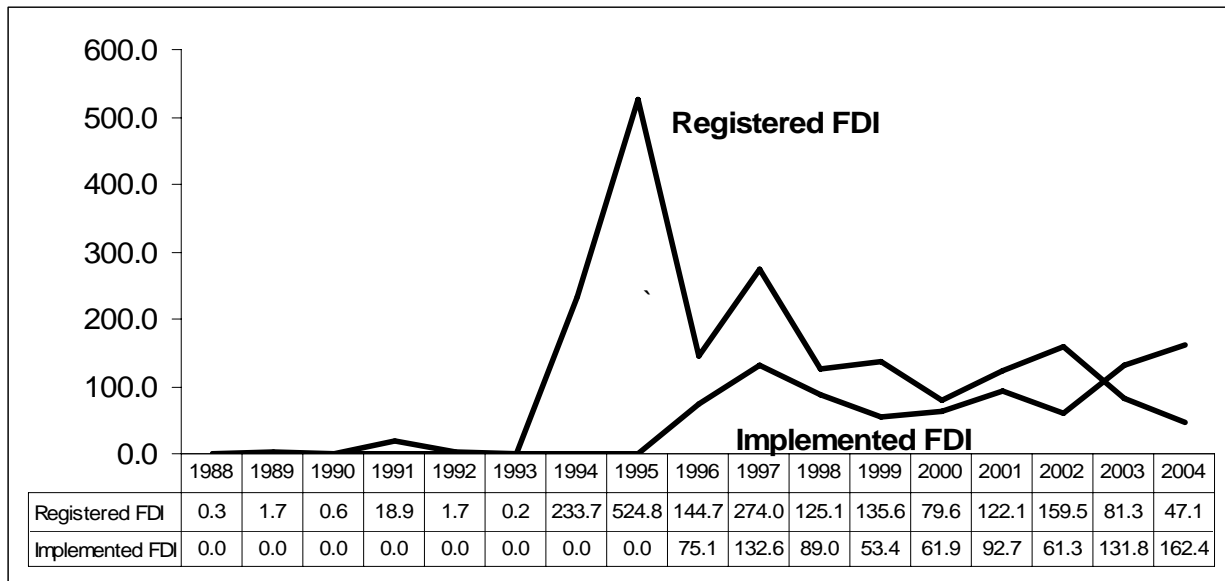
Source: MPI. The FDI data in this table are not adjusted for dissolved and expired projects.

Table 3: Implemented FDI in Clothing Compared to Total Implemented FDI from 1998 to 2004 (US\$ millions)

	1998	1999	2000	2001	2002	2003	2004
Clothing	84	97	102	141	198	176	204
Total implemented FDI	2,375	2,537	2,420	2,450	2,591	2,650	2,850
Share of clothing in total implemented FDI	3.5%	3.8%	4.2%	5.8%	7.6%	6.6%	7.2%

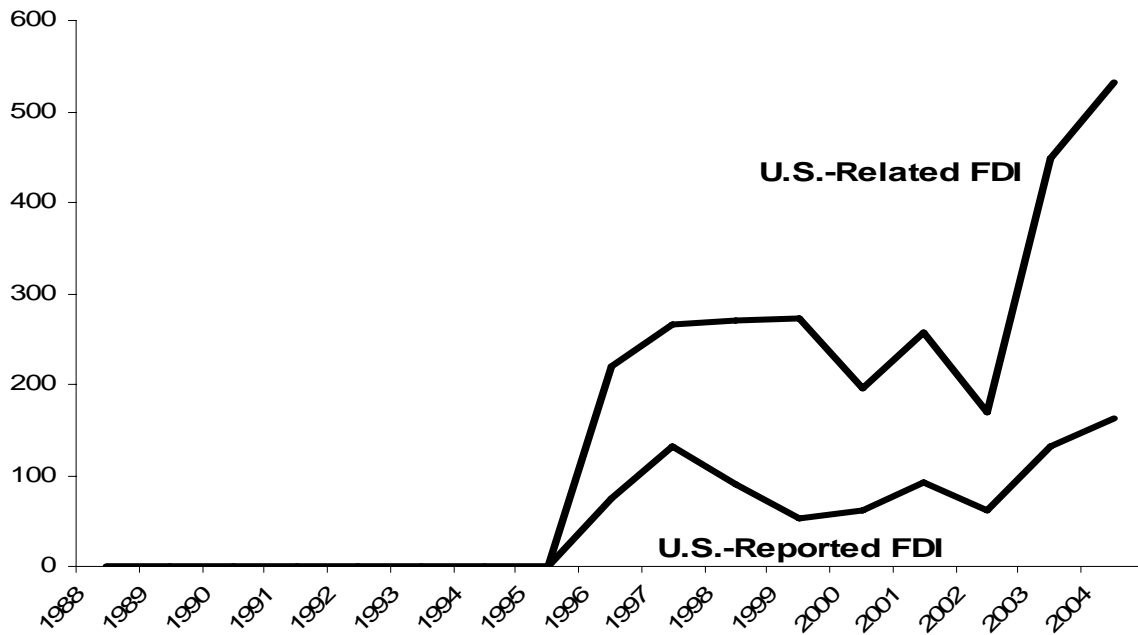
Source: MPI. The FDI data in this table are not adjusted for dissolved and expired projects.

Figure 3: Reported Registered and Implemented U.S. FDI from 1988-2004 (US\$ millions)



Source: MPI. The FDI data in this figure are not adjusted for dissolved and expired projects.

Figure 4: Implemented U.S. FDI (US\$ millions)



Source: MPI. The FDI data in this figure are not adjusted for dissolved and expired projects.

Table 4: U.S. FDI by Economic Sector (1988 through Dec. 31, 2004 – US\$ millions)

U.S.-Related FDI - I					U.S.-Reported FDI - II				
No.	Sector	No. of projects	Initial registered FDI	Implemented FDI	No. of employees	No. of projects	Initial registered FDI	Implemented FDI	No. of employees
I	Industry and construction	176	1751	2208	12637	149	822	519	6281
1	Heavy industry	92	648	385	3073	80	487	234	2085
2	Food processing	19	557	693	2566	16	67	9	283
3	Oil and gas	8	219	864	1430	6	124	232	780
4	Construction	15	196	146	1530	11	82	26	214
5	Light industry	42	131	120	4038	36	63	19	2919
II	Agriculture-Forestry and Fisheries	26	198	87	873	24	153	62	863
6	Agriculture and Forestry	24	187	82	770	22	142	58	760
7	Fisheries	2	12	4	103	2	12	4	103
III	Services	65	653	339	3343	42	316	149	1297
8	Hotel and tourism	13	267	72	785	5	73	3	0
9	Culture, healthcare, education	12	136	35	1007	11	86	34	1003
10	Banking and finance	10	11	103	915	4	65	37	0
11	Transportation, communications and postage	12	67	60	289	10	44	46	163
12	Apartments and buildings	2	37	41	37	1	16	8	7
13	Others	15	33	25	310	10	27	19	124
14	EPZ and IP development	1	5	3	0	1	5	3	0
	Total	267	2602	2634	16853	215	1291	730	8441
Understatement (I-II)						52	1310	1904	8412

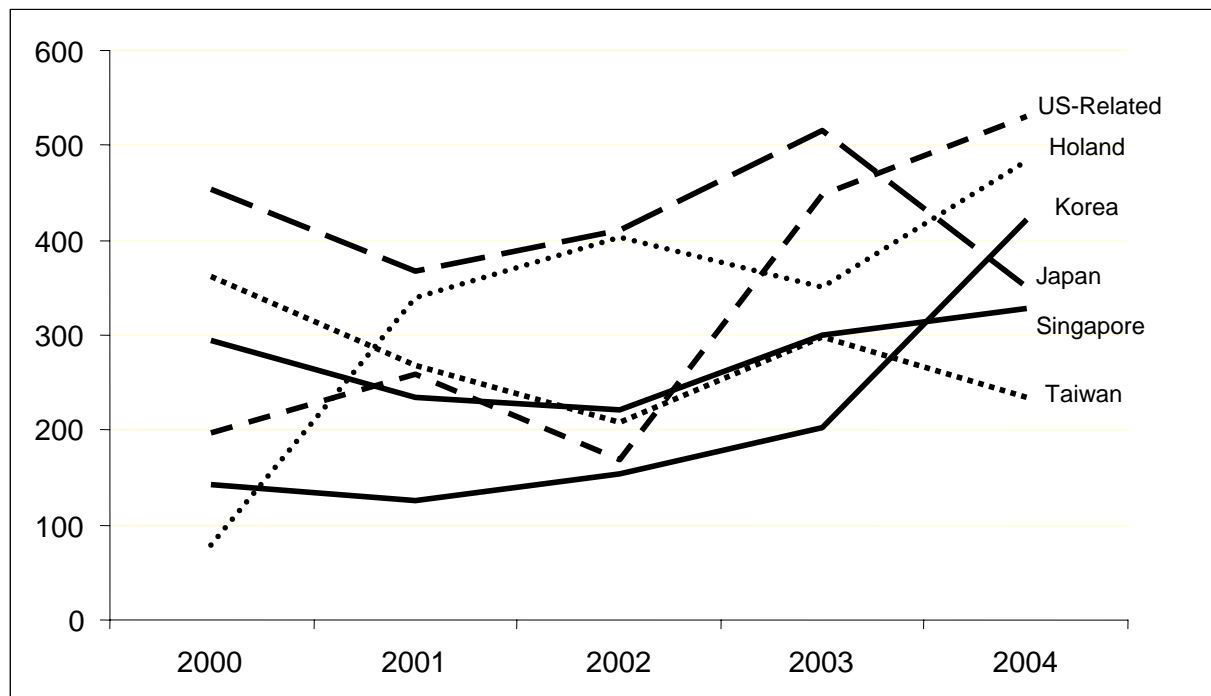
Source: MPI. Initial registered capital reported in this table is registered capital at the time of establishment, which does not include subsequent capital changes. Implemented FDI is for active projects, which excludes dissolved and expired projects.

Table 5: Growth Rate and Share of U.S.-Related Implemented FDI (US\$ millions)

Year	U.S.-Related FDI			Reported U.S. FDI			Overall FDI	
	FDI	Growth rate	Share in overall FDI	FDI	Growth rate	Share in overall FDI	FDI	Growth rate
1996	220		8%	75		3%	2923	
1997	266	21%	8%	133	77%	4%	3218	10%
1998	271	2%	11%	89	-33%	4%	2375	-26%
1999	274	1%	11%	53	-40%	2%	2537	7%
2000	196	-28%	8%	62	17%	3%	2420	-5%
2001	258	31%	11%	93	50%	4%	2430	0%
Pre-BTA geometric means		3.2%			4.3%			-3.6%
2002	169	-35%	7%	61	-34%	2%	2591	7%
2003	449	166%	17%	132	116%	5%	2651	2%
2004	531	18%	19%	162	23%	6%	2850	8%
Post-BTA geometric means		27.3%			20.5%			5.5%

Source: MPI. The FDI data in this figure are not adjusted for dissolved and expired projects. This is why cumulative reported implemented FDI in this table exceeds cumulative registered implemented FDI in Table 4.

Figure 5: Implemented FDI from the Six Biggest Investors in Vietnam (US\$ millions)



Source: MPI. The U.S. trend line is for U.S.-related implemented FDI. Other countries' trend lines are for reported implemented FDI.

Table 6: Implemented FDI by Country from 2000 to 2004 (US\$ millions)

No.	Countries	2000	2001	2002	2003	2004
1	U.S.-Related	196	258	169	449	531
2	Holland	79	339	403	350	483
3	Korea	142	125	154	203	421
4	Japan	454	367	411	515	350
5	Singapore	294	235	221	300	328
6	Taiwan	361	269	208	298	235
7	France	76	137	109	169	152
8	Hong Kong	195	87	118	76	145
9	Thailand	35	54	77	67	76
10	Mauritius	45	85	39	94	62
11	China	26	27	49	31	51
12	Russia	216	169	175	74	46
13	Cayman Islands	18	30	40	39	46
14	BVI	123	108	113	46	45
15	Australia	24	14	24	30	41
	Others	265	311	390	226	206

Source: MPI.

Table 7: Resident Country for FDI from U.S. Overseas Subsidiaries (1988 through Dec. 31, 2004, US\$ millions)

No.	Resident country for U.S. overseas subsidiaries with FDI to Vietnam	No. of projects	Registered FDI	Implemented FDI
1	Singapore	13	562	806
2	Holland	4	175	115
3	Hong Kong	8	138	109
4	British Virgin Islands	7	74	23
5	Bermuda	3	69	157
6	Mauritius	1	65	618
7	Switzerland	2	60	1
8	Cook Islands	1	50	0
9	Cayman Islands	1	37	41
10	United Kingdom	2	31	15
11	Ukraine	1	16	12
12	Taiwan	4	12	8
15	Japan	1	0.5	0.0
	All other	1	9.7	1.8
	Total	52	1,299	1,904

Source: MPI.

Table 8: U.S. Investment by Form (1988 through Dec. 31, 2004 – US\$ millions)

U.S.-Related FDI - I						U.S.-Reported FDI - II			
No.	Form of investment	No. of projects	Registered FDI	Implemented FDI	No. of employees	No. of projects	Registered FDI	Implemented FDI	No. of employees
1	100% foreign owned companies	192	1636	1104	10253	159	853	267	5811
2	JVs	59	732	662	5080	42	300	229	1760
3	BCCs	16	234	867	1520	14	139	235	870
	Total	267	2602	2634	16853	215	1291	730	8441
Understatement (I-II)						52	1310	1904	8412

Source: MPI. Registered capital reported in this table is initial registered capital at the time of establishment, which does not include subsequent capital changes. Implemented FDI is for active projects, which excludes dissolved and expired projects.