FOREIGN DIRECT INVESTMENT IN VIETNAM

THE CASE OF AMERICAN FIRMS

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In recent years American firms have rapidly increased their presence among foreign firms in Vietnam. By 1999, American investment was among the top ten largest in Vietnam. By the end of 2003, there were about 400 American firms in Vietnam with a total registered capital amounting to US$1308 million, accounting for 3.54% of the total registered FDI in Vietnam (MPI report, September 2003). However, compared with other foreign investors in Vietnam, American investors do not appear to be very successful and they went out of the top ten largest in Vietnam by the end of 2003. The ratio of disbursed to registered capital is very small, only about 26%, and recently some American firms in Vietnam have had to either withdraw their capital or increase their capital. These phenomena indicate not only a great loss on the part of American investors but also a disadvantage to Vietnam. They have had a notably negative psychological impact on other foreign firms and investors who were interested in investing in Vietnam.

The above situation has raised important questions about the nature of Vietnam’s FDI regime and related policies and the evolving strategic responses of overseas-based transnational corporations (TNCs), especially American ones? What constrains and other challenges have the Vietnamese authorities imposed on American firms? Have the American firms made bad judgments or is the Vietnamese business environment to blame? From the standpoint of American investors, what advantages are there to invest in Vietnam? How have government policies and practices affected their business strategies, both at time of entry and during subsequent operation? These questions are especially important in the context of the recently signed bilateral trade agreement between Vietnam and the United States.

The proposed study examines the interactions between Vietnam’s FDI regime and related policies and the overseas investment strategies of American firms. It also analyzes the strengths and weaknesses of American firms in comparison with other foreign firms in Vietnam, especially those of Japan.

1. Vietnam’s FDI policies and overseas-based strategies of American firms

1. Vietnam’s FDI policies

In line with its broader program of economic reform, the National Assembly of
the Socialist Republic of Vietnam has passed the Foreign Investment Law in Vietnam (December 29, 1987). The law basically addressed the weaknesses of the 1977 regulation and provided more favorable conditions for foreign investors in Vietnam. At the time of issuance, the law was evaluated to be attractive when compared with similar laws of other regional countries.

Unlike the 1977 regulation, the 1987 law guaranteed not to confiscate and nationalize legally owned assets of foreign investors. It also committed to provide equal and fair treatments to foreign investors. There are no maximum limits on the capital share contributed by the foreign investor in the form of joint-venture enterprises but the minimum must not be below 30% of the invested capital. The law also allowed foreign investors to choose among investment forms which are then prevalent regionally and internationally: the business cooperation contract (BCC), joint-venture enterprise (J/V) and 100% foreign capital enterprise. Profit tax rates are much lower which vary around 15 - 25% of the profit. Moreover, foreign invested enterprises shall be liable to maximum profit tax exemption period of 2 years from that beginning with profitable business, and a 50% profit tax reduction during 2 subsequent years. In some cases, profit taxes are even lower (10%) and the periods of profit tax exemption and reduction longer (4 years). Furthermore, the law permits foreign investors to remit profit home with the tax rate of 5 to 10%.

It is evident that the Foreign Investment Law (1987) is a breakthrough when compared with the 1977 regulation. It reflects the fact that Vietnam has taken a more transparent, more pragmatic conception about the role of FDI on the development process of national economy. Nevertheless, after an implementation period, the law has revealed a number of constraints, causing troubles to foreign investors. For example, the law does not allow private sector to directly enter business cooperation with foreign investors. Domestic investors therefore have to group to become a joint-venture side while foreign investors have to do the same thing to become a foreign side. The law does not permit to account interests paid on loans as costs. Contribution to equity by Vietnamese side is chiefly land use right. In addition, other documents supporting the implementation of the law were not issued adequately in a timely manner. For example, the Decree No. 139 by the Minister Council which provides detailed instruction on the law was only issued 10 months after the other economic laws had been issued, making the foreign investment legal framework in Vietnam inconsistent and risky.

In 1990, the Foreign Investment Law was revised with important changes made. Most notable of all are: liabilities limited companies or shareholder companies are allowed to cooperate with foreign investors (excluding some special cases); profit tax privileges accompanies with some specific conditions (technology transfer, proportion
o goods produced for export, volume of labor etc.); interests are accounted as investment costs... Despite these changes, the revised law failed to get rid of such limitations as: investment forms not being diversified, the absence of the stipulation on the compensation of the Vietnamese Government in case it causes damages to the capital and assets of foreign investors, too strict control on bank account of foreign invested companies, unsuitable period duration... Hence, the National Assembly of Vietnam had to revise the Law on foreign investment for the second time in December 1992. The amendments and supplements cover the following matters: definition of Vietnamese side consisting of one or more businesses of different economic sectors, establishment of export processing zones (EPZ) and business activities in EPZ, the revised law's more concrete and focusing in some definitions. Particularly, it also provides regulations on new types of attracting and encouraging investment capital. Since 1992, along the course of revising and amending laws and other documents regarding foreign investment in Vietnam, regulations on the repatriation of investment capital or profits tend to be increasingly strict and complicated. As a result worries have been raised among investors since 1995-1996, and the number of projects approved went down enormously at the end of 1996.

In order to solve the above problems and make the law more attractive, in November 1996, the National Assembly of Vietnam adopted the new law on foreign investment by basically amending and supplementing the law on foreign investment 1987 and its two revisions in 1990 and 1992. In addition, the National Assembly has also revised and adopted many important laws such as commercial law, company law, law on private companies, etc.

Key amendments made under this revision include the followings: investment privileges are linked with development orientations of the economy, foreign investors are allowed to contribute capital in Dong (Vietnamese currency) which has foreign currency origin. Build-Operation-Transfer (BOT) form is diversified with BTO and Build-Transfer (BT); more autonomy given to foreign enterprises; investment encouragement areas are enlarged (hospital, training...); licensing process is shortened and simplified; state management on foreign investment is more decentralized and concrete regulations on the areas and fields where foreign investment is encouraged; areas and fields where foreign investment is restricted; new regulations on the reduction and exemption of profit tax, for example, profit tax can be exempted for at most 4-8 years; exemption of import duties on machinery and transport vehicles specified for investment projects; reduction and exemption of rents on land, water and sea area used in investment projects under the form of BOT, BTO, BT; investment projects in mountainous, remote and hard-up areas; regulations on...
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diversification of investment forms; legalization of industrial zones; limiting the use of consensus voting in making decisions through the Board of Management; reducing the time for evaluating and licensing to 60 days.... Together with these changes, a raft of decrees and regulations has been announced to provide specific guidance on the implementation of the law.

Recently, under the pressure of a sharp drop in FDI in Vietnam and of an increasing competition from improvements of investment environments in regional countries, the foreign investment law has been revised for the forth time in June, 2000. The latest revision has included two new articles and revised 20 articles in the light of developing and expanding the stipulation of the prevailing investment law. The revision mainly deals with three issue areas. Firstly, it includes the regulations which help to minimize difficulties, troubles and operation risks of foreign invested companies. The revisions are on such issues as foreign currency balance, opening of bank account in foreign countries, use of land as collateral for bank loans, land clearance, without recourse principle, guarantee by the government and application of foreign laws. In this revision, the law has been revised in a way that enlarges the autonomy of foreign invested capital. The direct intervention of the government on day-to-day operations of enterprises is removed, setting up a legal framework for both domestic and foreign enterprises to be suitable with international practice. Changes are also made on consensus principle, a transform between investment forms, suspending operation and expatriation of foreign invested enterprises and expatriation of business cooperation contact, allocation of various funds and reserves, minimization of investment procedures. Third, the revision also deals with three issues regarding import tax exemption, remittance of profit abroad and loss transfer. However, the have not been any further guiding circles since then. Thus, investors are still unwilling interested in investing in Vietnam. The traditional worry is that the law is fair, open and clear, while sub-laws try to limit incentives and make it difficult to implement the law.

In brief, the legal framework of foreign investment in Vietnam is characterized with the following distinguishing features: temporary laws, inconsistency, fast variable regulation, discrimination (between foreign firms and local companies), non-transparency in enforcement, inconsistency with international laws and practices. The constraints have eclipsed investment incentives and discouraged foreign investment capital flowing into Vietnam.

2. Overseas - based strategic American firms

Firms have been able to sustain rapid sales growth, reduce product costs and improve quality by entering new markets and setting up operations on abroad. These firms have to choose the most effective
entry mode strategy so that they can remain competitive advantages on foreign market and generate additional profits. The appropriate entry strategy of the firms normally considered from the mode of entry and results of superior market and financial performance. However, this strategy can vary because of different firms in different countries.

According to the firm studies (Porter 1987; Woodcock, Beamish and Makino, 1994), the selection of an appropriate entry mode strategy is crucial and affects the overall success of an investment in the foreign markets. The recent study (Somkiat Mansumitrchai, Michael S. Minor and Sameer Prasad, 1999), examined three entry modes of American and Japanese firms: startups (greenfield investments), acquisitions (the purchase of sufficient stock of an already existing firm in order to gain control) and joint-venture. The results of the study showed that the mean number of startups of the US firms was not higher than that of Japanese firms, whereas the mean number of acquisitions of the US companies was greater than the mean number of acquisitions made by Japanese firms. And, the mean number of the US joint-venture was less than that of Japanese ones. This study concluded that the US firms tend to use acquisitions, followed by joint-venture as part of their entry mode strategy. Startups seem to be the least attractive option. Japanese firms, on the other hand, tend to prefer joint-ventures followed by acquisitions. Again, startups remain the least-preferred option.

Based on the results of the study as mentioned above, it is clear that American firms are still not attracted by the FDI policy of Vietnam, because the Vietnam's FDI policy tend to favor foreign firms to invest in startups and joint-venture, whereas not permit or encourage acquisitions. Therefore, these policies are likely to encourage Japanese firms than that of American firms. The fact that, Vietnam's FDI policy has been emphasizing the greater local control of operations of foreign firms, it likely to result in a higher proportion of joint-venture set up.

The other research works found that American are more inclined to take risks than the Japanese (Hofstede, 1980). In order to minimize risk, Japanese firms are more likely than American firms to team up with local companies (Pan, 1994) and to incrementally invest in new markets (Kagono, Nonaka, Sikakibara and Okumura (1985). This character is likely to fit American doing business with the high risky environment in Vietnam. The work (Pan, 1994) also found that there was different character in the management styles between Japanese and American firms. Japanese managers prefer detailed negotiations with potential partners, whereas American firms desire a faster process, it means that the American firms prefer quicker implementation. This personality can generate problems for American investors in Vietnam, because it is not easy to find the right local partners in the short time with the current condition of Vietnam.
The next important characters that need to be considered are the business strategy. This strategy is including the two main aspects: production and marketing activities (Charles, ZeisAhmad Ahmadian, Hailu Regassa, 2000). Based on the results of competitive study between the American, Japanese and European firms, these authors concluded that Japanese firms did a quality control of products better than that of American and European firms, whereas this issue is believed to be an important corporate strategy. The other survey found that board of directors of American firms is not concerned much about quality issues. Many U.S firms have initiated quality programs, but they also report that they are not being implemented properly. Some use quality audits to assess the results of their programs (Bowles, 1993). In Vietnam, consumer’s goods made by Japanese firms are likely to favor than those of American and European firms because of the reputation about the high quality products of Japanese firms.

Marketing strategy is very important for the firms. A number of researchers found that there were different characters in this issue among American, Japanese firms. With a strong character of seeking for natural resources and low cost of inputs, Japanese investment is considered as “input-orientated” and trade promotion. Conversely, main character of American investors is looking for the size of local market as “market-orientated” and therefore it reduces an international trade (Kojima, 1978). If this is accepted, marketing strategy of Japanese firms is more suitable than that of American ones in the market conditions of Vietnam. Because the current Vietnam’s FDI policies are a strong support for foreign firms with the high rate of exported products and the local market is small (due to low income of consumers). However, in the long term, this situation will be changed toward more liberalization of FDI policies and the increase of local market power. This is an important reason to keep American investors staying in Vietnam.

The other content of marketing strategy is marketing activities. They have been defined as factors of customer orientation, competitor orientation and inter-functional coordination. Some researchers found that Japanese firms were more custumers oriented in comparison to American or European companies and have thus been very successful in the countries they have invested into (Deshpande, Farley, and Webster, 1993). In Vietnam, this character is reflected clearly, Japanese investors strongly adapt their marketing to differences in customer tastes, competitors, product specifications, etc., while American and European ones often transfer “marketing technology” into Vietnam with a little adaptation. Therefore, many of those technologies are not suitable with Vietnamese culture (Trung Duc and Tien Hai, 1999). Recently, a number of American firms have been
changing the way of marketing for more suitable with Vietnamese consumers such as Ford, P & G, Motorola and Pepsi/IBC.

The strategy on customer suppliers is also different between American and Japanese firms. A recent survey found that the performance of internal suppliers is disappointing in terms of quality, on-time delivery, cost and cooperation. Survey results including written comments indicate that American firms are likely to reduce the number of suppliers and prefer to have single or dual suppliers. It appears that the customer-supplier relationship is deepening (Hong Y Park, C. Surender Reddy, and Sam Sarkar, 2000). The conclusion of survey suggested that the customer-supplier relationship has been deepening in recent years. Buyers are working with fewer suppliers. They do not change their suppliers frequently. They involve their suppliers at the early stage of product development and share technology and information. And the technology is an important factor in establishing buyer-supplier relationships. With this character, it is not easy for American firms to set up the customer-supplier relationship in Vietnam because almost local suppliers do not satisfy the requirements of American firms. Subsequently, the incentive of FDI policies for foreign investors in expanding backward and forward linkages is not attractive for American firms.

II. The competitive advantages of American firms in Vietnam

After the US government left the economic embargo against Vietnam in 1994, many American investors quickly came to Vietnam and there were 30 American representative offices were established within one day after the first day of this event (George C. Herring, 1996). It showed that an interest within the American business community about investment opportunities in Vietnam has ballooned. However, as new comer among foreign investors, American firms need to aware their competitive advantages in Vietnam. This matter should be considered in the two aspects: business environment and contesability of the firms.

1. The business environment

The business environment can be understood that it includes all factors that influence a business process of investors. Among these factors, we will focus on some main factors relating to the competitive advantages of American firms in Vietnam such as government policies, transportation costs, socio-cultural similarities and/or differences between Vietnam and countries of foreign investors, and customs of local consumers.

Among home government policies, the US government has been the lowest to support economic engagement with Vietnam. (Mark Mason, 1998). This support has developed only slowly since the start of doi moi (economic reform) 1986. However, it still remains quite limited and only in the forms of humanitarian aid. The US ambassador to Vietnam, Mr. Pete Peterson, in the interview with the Vietnam Economi
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Times, said "we are forbidden to give any amount of development aid for the Socialist Republic of Vietnam. And we just only provide the humanitarian aid, with amount of 3 million USD yearly (VET/Supplement, July 1997). So, the US government still does not provide export and investment insurances for American firms in Vietnam. In opposition, for Japanese investors, their government strongly supported them to Vietnam by giving investment insurances for Japanese investors and providing a lot of development aid (ODA) for Vietnam. Moreover, unlike with the US government, the Japanese government often links their development aid with improvements of investment conditions for Japanese investors in Vietnam (ODA report, IMP 2000). Therefore, these policies strongly promoted Japanese firms to Vietnam. Thus, American firms have less competitive advantages than Japanese ones in Vietnam.

From the Vietnam's government policies, there is no discrimination between foreign investors. The results of recent survey showed that a number of American and Japanese managers responded mostly the same rates of answers in receiving the same investment incentives and performance requirements from Vietnamese government (Mark Masson, 1998). However, in term of entry strategy, due to investment incentives of Vietnam focus on the promotion of export and backward-forward linkages, so Japanese firms are likely to more competitive advantages than American companies.

Although all foreign investors are treated equally, but in term of political viewpoint, the Vietnam government is still careful with American firms, especially those investing in the key industrial sectors such as telecommunications, energies and information technology. Therefore, in practice, many American investors have been facing with obstacles of unwritten policies. This problem was reflected in the advices of Mr. Ly Quang Dieu, former prime minister of Singapore, to Vietnam government as follow "you are treating the American investors as like as the war time. You invite them coming but at the same time, you also ambush them. As the result, they withdraw their capital out of Vietnam (Do Duc Dinh, 2000).

Recently, the Vietnam-US bilateral trade agreement has been signed, many American investors hope that it will create the favorable conditions for them in competing with other foreign firms in Vietnam. It is, however, possible to suggest these changes are small (in the short run) because the US government still does not provide the necessary insurances as American investors needed. Nevertheless, in the long run, American firms may have more competitive advantages in a number of economic sectors such as telecommunications, energies and oil and gas industries.

Transportation costs are very important issues for the firms. The fact
that, almost all Japanese firms in Vietnam are relocated within a region, whereas American companies coming from a long distance, therefore transportation costs of Japanese firms are likely to lower than that of American companies. Nonetheless, this advantage has been changing since the Asian financial crisis in 1997 and the event of September 11, 2001 because of many American firms comes to Vietnam from the relocation of their production network in the Asia (Nguyen Minh Long, 2000).

The differences and similarities in socio-cultural issues between Vietnam and countries of foreign investors are also very important for increasing or reducing the competitive advantages of foreign firms in Vietnam. In these issues, American investors are likely to have less competitive advantages than Japanese and Asian investors, because the socio-cultural characters of these investors are quite similarities with that of Vietnamese people (Do Duc Dinh, 1999). For example, Japanese and Asian investors often have good experiences (personal relationships, patient and indirect words) in contacting with Vietnam government officials and local partners, while American investors prefer to straightforward and quick ways in working with Vietnamese partners. Yet, this character is likely to not suitable with Vietnamese culture.

In term of consumer customs, American products are known as high quality and durable goods, therefore they are interested by Vietnamese consumers. Yet, the design and ways of product delivery are not suitable with the taste and buying way of Vietnamese people. In contrast, Japanese product mostly satisfies the requirements of Vietnamese consumers, in which especially about the reputation of quality and designs of their products. It can be said that, in the short run, American firms are not likely to have the competitive advantages on the consumer customs in Vietnam, especially in comparison with Japanese companies.

2. Contestability of the firms

The concept of "contestability" emphasizes the role that potential competition plays in disciplining the behavior of firms (WIR, 1997). It consists of main factors such as finance, technology (including R&D), and managerial method. In this part, we will analyze what contestability of American firms in Vietnam.

American investors have been considered as a great potential in financial sources among foreign investors in the world. Therefore, they have more competitive advantages than other foreign firms in implementation of their long term business strategy in Vietnam. In the fact that, there are many American firms, such as Ford, P & G, Coca-Cola and IBC, who were accepting heavy financial loses in short term so that they want to obtain a larger proportion of local market and monopoly positions in Vietnam in the long term. Almost all American investors are looking for long term profits rather than
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short term interests in Vietnam. The survey results of AMCHAM and JETRO (1996) showed that 80% of American managers accepted not profitable in the short run. On the other hand, 56% of those expected to profitability in the long run. The results of firm study conducted by IWE in 2000 also strongly supported this trend.

Unlike with other foreign investors, US firms often transfer high technologies to recipient countries in order to obtain monopoly positions of new market. Thus, American investors have more competitive advantages in the hi-tech industries in Vietnam such as telecommunications, energies, oil & gas and information technology. These advantages will be stronger after the bilateral trade agreement fully implemented. And this feature has been appraised is that that "American firms are strong ones; they have high technologies and great potential financial resources, so they have strong competitive advantages in Vietnam" (Thomas O'Dore- Representative of CIGNA and president of AMCHAM in Hanoi).

Comparison with other Asian investors, managerial method (control mechanisms) of American investors is not likely to be considered as competitive advantages in Vietnam. According to the recent studies showed that American firms often bring their modern managerial techniques into Vietnam (IWE, 2000 and Le Danh Doanh, 2001). These techniques are highly characterized by using the modern communication system- telephone calls, e-mail, internet connections or computer files in their control mechanisms (Sarah Boehle, 2000), whereas these factors are still very poor and high cost in Vietnam.

On the other hand, the managerial method used in American firms in market economies is still new to Vietnam because of the differences in institutional, organizational and cultural environment. Consequently, it may not be acceptable to the Vietnamese employees (managers) and requires extensive training of local employees before they can be effectively used. Therefore, the introduction of such techniques may be limited and costly or not function efficiently. To that extent, managerial method of American firms is not likely to compete in Vietnam.

In short, among foreign firms in Vietnam, American investors are likely to have strong competitive advantages in term of financial resources and technologies, while have lower contesabilities about managerial method. However, in the long run, American firms will increase their contesability in comparison with other foreign competitors because of the improvements of business environment in Vietnam.

III. Conclusions

This study has found a number of answers as follows: first, Vietnam's FDI policies are more incentives and non-discrimination among foreign investors. However, they are not synchronous, stable
and transparent. These constraints have eclipsed investment incentives and discouraged foreign investment capital flowing into Vietnam. Moreover, they also created many troubles for foreign investors in rearranging their business strategies in this country. Therefore, it can be concluded that the legal framework and related policies governing FDI in Vietnam is a potentially lucrative but high risky opportunity for foreign firms, especially American companies.

Second, the business strategy of American firms is not likely to suitable with the current conditions of business environment in Vietnam. However, in the long term it will be better with the improvement of business environment in this country, especially when the BTA will be fully implemented. Therefore, American investors must be careful with this character in making their business strategy in Vietnam.

Third, Vietnam will be more attractive country for American investors if they have strong supports from the US government and appropriate business strategies. In addition, they should be patient with officialdoms and the ways of doing business in Vietnam. It is suggest that American firms will have strong competitive advantages in the high-tech industries in Vietnam.

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Trước các công ty nước ngoài đang hoạt động ở Việt Nam, các công ty Hoa Kỳ được đánh giá là có tiềm năng đầu tư lớn nhất. Tuy nhiên, đến nay, đầu tư của các công ty này ở Việt Nam còn rất hạn chế, chưa được xếp vào 10 nước có đầu tư lớn nhất (top ten) ở Việt nam. Thực trạng này đang đặt ra nhiều câu hỏi: hạn chế này là do các tác động của chính sách đầu tư của Việt Nam hay do bất lợi của môi trường đầu tư của họ. Trên cơ sở phân tích so sánh các đặc điểm cơ bản trong chính sách đầu tư của nước ngoài của Việt Nam với chiến lược đầu tư và lợi thế cạnh tranh của các công ty Hoa Kỳ ở Việt Nam, bài viết đã đưa ra những nhận định quan trọng: chính sách đầu tư của nước ngoài của Việt Nam thông thoáng nhưng ít ổn định, thiếu minh bạch và hiệu lực thấp trong khi chính sách đầu tư của các công ty Hoa Kỳ lại thích hợp với môi trường chính sách ổn định, minh bạch và tính hiệu lực cao. Mặt khác, trong khi các công ty của Hoa Kỳ thường quan tâm đầu tư dựa trên hình thức 100% vốn đầu tư nước ngoài thì chính sách đầu tư của nước ngoài của Việt Nam lại thiên về khuyến khích các hình thức liên doanh, do đó thường hạn chế các công ty của các nước châu Á (đặc biệt là Nhật Bản) hơn là các công ty của Hoa Kỳ. Hơn nữa, do sự khác biệt quan trọng về văn hóa và phương thức quản lý, kinh nghiệm của các công ty Hoa Kỳ đã gặp nhiều rủi ro hơn các công ty của Nhật Bản và các nước châu Á. Bài viết đã đi đến kết luận: chính sách đầu tư nước ngoài của Việt Nam tuy ngàng rộng và thông thoáng nhưng vì ít ổn định, kém minh bạch và hiệu lực thấp nên chưa hấp dẫn các công ty Hoa Kỳ. Ngược lại, so với nhiều công ty nước ngoài khác, đặc điểm hoạt động và chiến lược đầu tư của các công ty Hoa Kỳ có khả năng thích hợp với môi trường kinh doanh ở Việt Nam.