

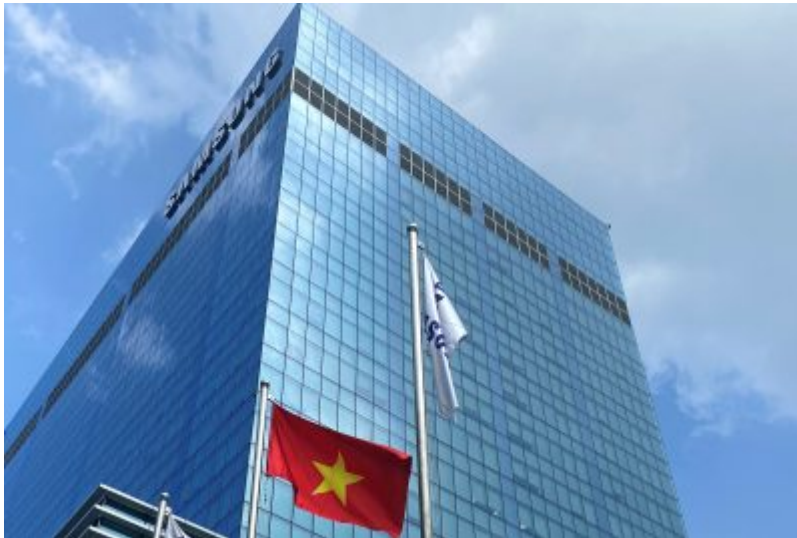
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Vietnamese firms are yet to find their competitive edge from FDI spillovers

Posted By *Trung Quang Nguyen* On 6 September 2023 @ 10:00 am In Finance, Investment, Labour, Vietnam | [No Comments](#)

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Vietnam is one of the great economic success stories of the past 35 years, having turned some US\$450 billion ^[1] in foreign direct investment (FDI) into major gross domestic product and other gains. The country remains a leading destination ^[2] for inward FDI, attracting global giants such as Samsung, Intel, LG, Toyota and Lego.



FDI is an attractive mechanism for developing countries because of its positive spillover effects, including technological advancements, skill transfers, managerial expertise and value chain integration. These spillovers occur through interactions with multinational enterprises (MNEs), from supplier relationships and through learning and competition within the domestic market. Over time, domestic firms grow more competitive, and this enables them to move up the value chain and compete with MNEs.

But available evidence suggests Vietnam has seen little of this spillover phenomenon. While Vietnam has observed some positive externalities such as job creation and record growth of the digital economy ^[3] over the past five years, these gains have not lived up to expectations and have failed to harness the country's full potential.

Local firms in the manufacturing sector have limited connections with FDI firms, making the economy overly reliant on FDI for exports. FDI generates over 70 per cent ^[4] of Vietnam's total export value — indicating a lack of comparable growth and development for local firms.

Domestic firms generally face challenges in enhancing their absorptive capacity ^[5] when FDI firms are present in the market, but it appears the Vietnam case is particularly severe. There are limited transfers of technology ^[6] from FDI companies to local firms and Vietnam's manufacturing sector has notably low productivity ^[7].

Only a limited number of Vietnamese firms ^[8] have managed to upgrade their position in the global value chain. As a result, their roles are mainly confined to providing input materials or low-value-added tasks, leading to fragmented and inefficient ^[9] linkages and externalities. One senior Vietnamese employee at a supplier of Samsung stated that although such an arrangement can offer major benefits, these are only accessible to a small fraction of the approximately 900,000 enterprises in Vietnam. For instance, in 2020, Apple sourced AirPods from 21 suppliers ^[10] in the country, but none of them were Vietnamese.

There are several reasons for the limited spillover effects from Vietnam's major FDI flows.

Government policies have long appeared to focus more on quantity than on quality. Regulations on technology transfer were not strictly applied. Combined with public mismanagement in several cases, this has led to low-tech FDIs proliferating through the economy. A large number of FDI firms prioritise simple technologies to take advantage of Vietnam's market size and potential as well as the country's low labour costs ^[11].

Another reason spillover has been minimal is that firms in Vietnam have a relatively short history of development compared to their peers. The imposition of a nationwide command economy right after the country's unification in 1975 hindered the development of the private sector. Though this strategic mistake began to be corrected ^[12] with the introduction of the Doi Moi policy in 1986, Vietnamese enterprises still have less market experience compared to their peers in the region and their corporate governance ^[13] is much poorer as a result.

In addition, private firms encounter various challenges in Vietnam, notably accessing capital and formal loans ^[14]. To cope, many turn to informal channels with higher rates. High logistics expenses and petty corruption with government agencies hamper local firms' competitiveness on the global stage. Finally, there are still gaps between the government's ambitions and the reality of implementation management ^[15] in the public sector.

Many of these challenges are man-made and can be addressed through effective policies and disciplined implementation. Vietnam possesses unique advantages, including its strategic location in Southeast Asia, a young and adaptable population, a politically stable environment, impressive innovation performance, a thriving digital economy and an open economy with multiple free trade agreements.

To fully leverage these advantages and promote positive externalities, especially in building strong local firms, Hanoi should prioritise investment in human capital by implementing a comprehensive national training program on digital competence. This will facilitate the successful

implementation of the national 4.0 strategy ^[16] and support both the digital ^[17] and green ^[18] transformations.

Targeted and comprehensive investment in digital, transport, energy and other key infrastructure will also improve domestic firms' competitiveness and further motivate the workforce. This can be enhanced by promoting a more functional bureaucracy through better pay and accountability. Hanoi may look to others in Asia — Malaysia, Singapore, South Korea — to see the advantages of digitalising government services to promote business efficiency, as well as the benefits of digital disruption for emerging value chains.

Vietnam must also improve the business environment and establish a level-playing field by enacting laws pertaining to state-owned enterprises, and position Vietnam as a regional hub to attract MNE headquarters and research and innovation centres.

While Vietnam has been an attractive destination for FDI firms, local firms have not fully realised the desired benefits. Overcoming these hurdles with the right strategy in place can strengthen local firms and lead to greater success.

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