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Promotion of Investment and Economic Cooperation (KMB II) Project

Inputs and Strategy Approaches for the Promotion of German Direct Investment in Vietnam

Executive Summary

Report by

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The views contained in this study are those of the author and do not represent the opinions of the GTZ or the MPI.

Summary

Background Achieving the Vietnamese leadership's ambitious goals requires among other things a large influx of FDI to Vietnam – government planning is based on annual inflows of 1-2 billion USD. German direct investment to Vietnam is as yet relatively low. In order to support Vietnamese institutions in their efforts to convince more German investors to commit to Vietnam and in order to provide inputs for the new FDI promotion strategy, the present study will examine the following points:

- State and development of German direct investments worldwide
- Expected trends in German direct investment
- State and development of German direct investments in Vietnam
- Satisfaction and experience of German investors in Vietnam
- Interest shown by German firms towards Vietnam
- Institutional landscape of investment promotion in Vietnam, focusing on German investors and relevant institutions in Germany
- Means of FDI promotion
- Strategic recommendations for promoting FDI from Germany

The results of the study are based on surveys conducted among German investors in Vietnam as well as managers in Germany with an interest in Asia, numerous conversations with the most important multipliers and intermediaries, as well as visits to various investment promotion events.

German Direct Investment in Vietnam – an Overview

German direct investment in Vietnam remains very low There are currently approximately 30 German direct investments (depending on which statistics) in Vietnam. Slightly more than half of these are 100% foreign-owned enterprises and the rest are joint ventures (JV) with a cumulative investment level of between 70 and 118 million USD and between three and four thousand employees. In addition, numerous German firms have representative offices (c. 85) in Vietnam. Nevertheless, Germany is only twentieth on the list of countries bringing FDI to Vietnam. The inflow of FDI from Germany reached its peak in the mid-1990s before suffering a massive drop in 1997, even before the onset of the Asian crisis. Since 2001, a somewhat more positive trend can be observed once again. The regional distribution of investment is clearly concentrated in Ho Chi Minh City (HCMC) and the surrounding provinces of Dong Nai and Binh Duong, as well as in Hanoi. It is striking that the great majority of the German 100% foreign-owned enterprises (FOE) are to be found in the south. This can be attributed to the great importance of local good governance, as was confirmed in interviews with the enterprises, which certified the competence and willingness to cooperate of the authorities in the above-named southern provinces and identified these as important locational factors. The most important factor motivating German enterprises to invest in Vietnam to date has been the opening up of new markets, whereas only a few German investors chose the location in order to lower costs. Only in the clothing and shoe manufacturing industries is a small concentration of German production for export to be found.

Satisfied German investors in Vietnam Interviews with German investors and intermediaries in Vietnam painted an exceptionally positive picture of investment conditions for German investors in Vietnam. The climate for investment was judged to be good to satisfactory, with a clear tendency towards improvement. This positive mood was also expressed in the fact that 80% of the enterprises surveyed would invest in Vietnam again and that 70% plan to expand their Vietnamese activities. In

interviews, Vietnam's greatest advantage as a location was identified as its workers. Besides the low cost of wages, almost all managers emphasised the very high quality of the workmanship, the high working morale, loyalty, quickness to grasp new tasks and thoroughness, leading to high product quality and low failure rates. Together with low wages, this leads to higher work productivity and low unit labour costs. Interestingly, the worker factor is also highlighted by managers who are familiar with the situation in numerous other countries in the region from their own experience. Further important positive points for FDI are high political stability and the very good security situation. The development of local markets is also very promising. Indeed, the market for consumer goods is growing rapidly through the emergence of a dynamic middle class, which has led among other things to a surge in demand for brand products, making German products attractive as they are relatively well-known and liked. The domestic private sector is also developing dynamically and there is increasing demand for equipment and technology, and state investment in infrastructure is also experiencing a positive development. Vietnam occupies a strategically advantageous position within ASEAN and AFTA. In an analysis of the most important factors for business investment decisions, the situation in Vietnam is evaluated as positive or very positive in five out of ten factors. There is a clear need for improvement among some of the other five factors. None of these seem to be a reason for not investing in Vietnam, however.

***Need for
action
according to
investors***

Despite the generally high satisfaction of German investors, there continues to be a need for action to improve the investment climate. The most important points here are; dismantling bureaucracy, lack of transparency of regulations as well as corruption. There were also demands for lower telecommunication costs, tax reform - including lowering the income tax rate for Vietnamese staff in the higher wage brackets - and improvements in the country's infrastructure.

German Direct Investment Worldwide – Current Situation and expected Trends

***German
direct
investment
worldwide***

German direct investment worldwide amounts to c. 700 billion euros, shared across a total of almost 30,000 firms with over 4 million staff. A huge expansion in German fixed assets abroad took place between 1997 and 2001 and there was a shift from trade and processing industries towards investment companies and other financial institutions. The peak of German FDI activity was reached in 1999 and has decreased sharply since then, in line with the worldwide trend. The most important target countries for German investors remain within the EU and North America, followed by Eastern Europe and Asia. Within Asia, German firms have directly invested 38 billion euros, 9 billion euros of which are in Japan and 6,8 billion euros in China. At 70 - 118 million euros, less than 1% of German FDI to Asia is in Vietnam. A look at annual FDI flows indicates above all the high volatility of investment flows to Asia. The development of investment flows also underlines the importance of a country's political stability to be attractive to German investors.

***China as a
competitor***

A look at German FDI in China, currently probably Vietnam's biggest competitor in terms of FDI, reveals that half of annual investments from Germany - which lay between 322 and 822 million euros from 1995 to 2002 - went to processing industries, although the service sector is gaining in importance. In interviews with German managers, China as a location was seen to have an advantage in the areas of low-cost mass production, better supply industries and a substantially larger domestic market. Elements speaking for Vietnam during the survey were the significantly higher quality

of work, greater openness towards Germans, a higher quality of life for foreigners, the strategic position within ASEAN/AFTA and the diversification of risk.

Expected trends in German foreign investment A survey of German Chambers of Commerce and Industry (*Deutscher Industrie und Handelskammertag, DIHT*) revealed that a significant increase in FDI from Germany can be expected in the years to come – 38 % of all German industrial enterprises are planning foreign investment in the next three years. The following trends are of particular interest:

- Increasing interest in Asia
- A trend to relocate also capital and knowledge-intensive functions abroad
- The biggest tendency towards FDI in the clothing, electrical appliance production, vehicle building, electrical engineering and textile sectors
- Well-developed interest in FDI among medium-sized enterprises
- Clear south-north and west-east split among German enterprises in their tendency towards FDI
- Reports of a particularly high interest in Asia from some chamber of commerce districts, although a clear west-east split exists. East German enterprises show little interest in Asia.
- Cost reduction is a more frequent reason for FDI than the opening up of new markets.

Inputs and Strategic Recommendations for promoting German FDI

German investors' interest in Vietnam Since the massive drop both in German investments in Asia and FDI flows due to the global economic and stock market downturn during the mid-1990s, interest in Vietnam has been minimal over the last few years. In the meantime, more companies have been taking up the issue of FDI in the Asian markets, first and foremost in China. The demand for information about Vietnam has also increased, although it set out from a low level.

Vietnam hardly known in Germany as a location for investment Even though investment conditions in Vietnam are advantageous, the inflow of FDI from Germany is still low. This is due, among other things, to the fact that Vietnam is hardly known as a location for investment in Germany and still remains a country with a rather exotic image. Further, the great interest in China currently overrides attention paid to other Asian markets. Insufficient sources of information, reluctance (particularly on the part of medium-sized enterprises) to take the plunge in what seems such a geographically and culturally distant country, and a lack of know-how in tackling this step represent additional hurdles, with the search for business partners in Vietnam being the greatest obstacle. Many of the interviewees also lamented the fact that it was difficult to obtain information about investment conditions in Vietnam.

Improving FDI promotion useful and promising In sum, the evidence shows that investment conditions for FDI in Vietnam can now be classified as good. At the same time, both the tendency to invest and interest in Asia are increasing in Germany. Given that Vietnam hardly features as an investment location for German managers, however, few direct investments flow from Germany to Vietnam. For that reason, an improvement and intensification of FDI promotion for Vietnam would be useful and promising.

No comprehensive support for German investors on There are numerous German institutions dealing with the issue of FDI in Vietnam, some of which offer information and events on the subject. Only few promotion/information activities on investment in Vietnam have taken place in the last few years, however, and there has also been very little demand for such information. There are also numerous institutions offering

entering the market demand for such information. There are also numerous institutions offering support to German firms in their engagement to Vietnam. Nevertheless, there is no point of contact either on the Vietnamese or the German side offering comprehensive support to interested entrepreneurs, something which deters small and medium-sized enterprises in particular. Another point of criticism is that requests from Germany were not answered by many institutions, or the answers were of low quality.

FDI promotion necessary at different levels A certain allocation of tasks between the different institutions is in place. The focus of the relevant Vietnamese institutions is thus on marketing Vietnam as a location, whilst German institutions support entrepreneurs in choosing a suitable location, which might be Vietnam, and help them in carrying out their project there. On the Vietnamese side, the Ministry for Planning and Investment (MPI) is in charge of FDI promotion and is currently developing an FDI promotion strategy. In order better to market Vietnam as a location in Germany, activities are necessary at different levels:

	Possible Activities
Awaken interest in Vietnam/ Image improvement	<ul style="list-style-type: none"> • Advertising campaign • Better information of intermediaries in Germany • Improved public relations activities, media tours • Creation of a network for public relations work in Germany • Representative in Germany • Roadshows • Development and presentation of Vietnam's advantages as a location • Further improvement of the investment climate
Availability of information	<ul style="list-style-type: none"> • Production and distribution of suitable information materials • Improvement of existing websites • Publication of market studies • Availability of information materials for German intermediaries on the advantages of Vietnam as a location • Trips for entrepreneurs • Information events • Establishment of information centres in Germany • Cooperation with German sectoral associations and German firms established in Vietnam • Professionalisation of responses to requests in all relevant institutions • Qualifications for staff working in the field of investment promotion
Sectoral approach	<ul style="list-style-type: none"> • Identification of promising sectors • Production of sectoral studies • Pro-active approach to the further improvement of the investment situation in these sectors (action plan) • Cooperation with sectoral associations in Vietnam and Germany
Support of enterprises in preparing and implementing an investment	<ul style="list-style-type: none"> • Availability of information materials on the individual steps for market entry • Support in the search for business partners • Support in the search for a location • Support in registration and licensing • Advice in designing contracts • Lobby function vis-à-vis state institutions

Support for German investors The majority of the above-named activities must surely come from the Vietnamese side and are in many cases dependent on the cooperation of different German institutions as multipliers. On the German side, the expansion of information services for interested enterprises and support for their market entry would be desirable. Medium-sized enterprises report above all on difficulties in entering the market and on the need for comprehensive support. It would make sense for the institutions concerned to develop a common strategy as to how support for German enterprises in Vietnam can be further improved. Possibilities here would be the creation of a German Centre, for instance, or a variation on the concept such as a virtual German Centre concentrating on specific services, which the market does not offer, or a European Centre in cooperation with other European institutions.

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