



## **REPORT**

# **THE IMPACTS OF ASEAN COMPREHENSIVE INVESTMENT AGREEMENT ON MANUFACTURE, AGRICULTURE, FISHERY, FORESTRY, AND MINERAL EXPLOITATION**

**ACTIVITY CODE: ICB-1**

**Support to Vietnam's participation to ASEAN Economic Community**

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## **ABBREVIATIONS**

ACIA	ASEAN Comprehensive Investment Agreement
AFF	Agriculture-Forestry-Fishery
AFTA	ASEAN Free Trade Area
AIA	ASEAN Investment Agreement
AIG	ASEAN Investment Guarantee
APEC	Asia Pacific Economic Cooperation
ASEAN	Association of Southeast Asian Nations
CIEM	Central Institute for Economic Management
EU	European Union
FDI	Foreign Direct Investment
FTA	Free Trade Agreement
GDP	Gross Domestic Production
GSO	General Statistics Office of Vietnam
RCEP	Regional Comprehensive Economic Partnership
TPP	Trans-Pacific Partnership
USD	United State dollar
WTO	World Trade Organization

# 1. INTRODUCTION

## 1.1. Background

Since Doi Moi started in 1986, regional and international integration has been considered as one of the most important measures to promote the country's socio-economic development. The country signed a trade agreement with the European Union (EU) in 1992. The country then joined the Association of South East Asian Nations (ASEAN) and the associated ASEAN Free Trade Area (AFTA) in 1995, following by the membership of the Asia Pacific Economic Cooperation (APEC) forum in 1998.

The economic integration process has been accelerated since 2000. In 2000, Vietnam and the US signed the Bilateral Trade Agreement (VN-US BTA), the first most comprehensive trade agreement which exposed the former to higher standard of trade and investment liberalization. The years 2000-2006 also witnessed strong efforts by Vietnam towards deepening multilateral and regional economic integration. The country extended comprehensive preparations for accession to the World Trade Organization (WTO) whilst signing and implementing various free trade agreements (FTAs) under ASEAN framework such as ASEAN-China FTA and ASEAN-Korea FTA. The accession to the WTO in 2007 then further consolidated optimism of both the domestic community and foreign investors about Vietnam's growth prospect. Since then, Vietnam has signed and implemented more FTAs at the regional levels such as ASEAN-Australia-New Zealand FTA, ASEAN-Japan Comprehensive Economic Partnership, and ASEAN-India FTA. Other efforts have also been extended toward establishing the ASEAN Economic Community (AEC) by 2015.

Even at this stage, the country is actively engaged in negotiating several ambitious FTAs, such as the Trans-Pacific Partnership (TPP), EU-Vietnam FTA, the Regional Comprehensive Economic Partnership (RCEP), etc. The depth and scope of FTAs have been continuously expanded, from trade in goods to services trade and other new issues such as trade and investment facilitation, intellectual property right, etc.

In that context, the 39<sup>th</sup> ASEAN Economic Ministers (AEM) Meeting held in the Philippines on 23<sup>rd</sup> August 2007, taking into consideration of current and future needs for a comprehensive and robust investment environment in ASEAN, decided to revise the framework of ASEAN Investment Area (AIA) into a forward looking and comprehensive agreement – ASEAN Comprehensive Investment Agreement (ACIA), with improved features and provisions by taking into account the changing global business and economic landscape as well as the different stages of development within the ASEAN. The ACIA is also intended to shore up the sustainability of ASEAN towards its economic integration agenda under the AEC in 2015 and beyond. The ACIA was signed on 26<sup>th</sup> February 2009, and entered into force on 29<sup>th</sup> March 2012.

## **1.2. Scope of the Study**

Under the support of EU-MUTRAP, this study is implemented to identify the impacts of ACIA with respect to inward FDI on the five main investment sectors covered by the agreement (agriculture, forestry, fisheries, manufacture, and mineral exploitation) during the period of ACIA implementation 2012-2014 on national investment (both FDI and domestic investment), domestic production, exports and imports in the five sectors covered by the agreement. Due to data unavailability, the impacts of outward FDI (investment by Vietnamese investors abroad) are not subject of this study.

## **1.3. Methodology**

Measuring impacts in general and the ones brought by ACIA is not an easy task for several reasons. Firstly, as the ACIA implementation has been underway only for more than three years, the impacts may not be realised. An investment project often takes three to five years to finish its major construction and equipment installation. Secondly, during the same period, Vietnam also implemented trade and investment liberalisation committed in other global, regional and bilateral arrangements, as mentioned above. The outcomes that occur are synergy of all realised commitments. Furthermore, the rapidly changing world situation affected the extent ACIA was realised as well. Detailed data availability is another issue that makes the task difficult.

The methodology will be mainly tracking along those channels through which changes in investment from ASEAN are transmitted to the economy. Firstly, more favourable investment conditions in the selected sectors act as incentives to attract FDI to these sectors. These FDI projects will have so called horizontal impacts (or intra-sectoral), which can be positive or negative, on domestic investment in the same sectors. On one hand, domestic investors face a stronger competition from FDI in their sector. On the other hand, they may benefit from spill-over in term of new technology and managerial skills.

Secondly, through the so called backward linkage, FDI in the sector in consideration influences output levels of their input suppliers (both foreign-owned and domestic) in upstream sectors (vertical impacts). Through forward linkage, the FDI affects output levels of their foreign-owned and domestic buyers/users of their products in downstream sectors (another type of vertical impacts).

Thirdly, these changes in its turn may affect investment decisions, and consequently output levels, of both suppliers and users.

Fourthly, the changes in outputs are transmitted into exports and imports of the products of interest.

## **1.4. Structure of the Report**

The report starts with the summary of the ACIA, followed by an overview of FDI in Vietnam. Impacts of the ACIA implementation on FDI flows and domestic investment are discussed in Section 4. Section 5 estimates the impact of ACIA on domestic production. ACIA impacts on exports and imports are summarised in Section 6 and Section 7. Section 8 concludes the study.

## 2. ACIA SUMMARY

One of the four primary objectives of the coming AEC is to become a single market and production base with five core elements: the free flow of goods, services, investment, and labor, and the freer flow of capital. In accordance with these objectives, the ACIA aims at bolstering ASEAN investment by establishing a free, open, transparent and integrated investment regime for domestic and international investors throughout the ASEAN member states that supports the economic integration of the region before and after the ASEAN Economic Community integration in 2015.

In replacing its two precursors, the AIA and ASEAN Investment Guarantee (AIG) agreements, the ACIA attempts to establish a regime based on international best practices while expanding and reaffirming principles set down in the AIA and AIG. In doing so it provides comprehensive and clear definitions in line with existing international agreements, enhancing the attractiveness of ASEAN as a single investment destination. The ACIA improves the two earlier agreements in a number of areas by means of:

- Adopting international best practices that help protect investors and their investments and providing increased protections
- Following recent trends in international investment practices that encourage less restrictive investment regimes
- Including portfolio investment and intellectual property as well as broader definitions of investors and investments
- Allowing third-country nationals to benefit from the ACIA
- Encouraging a higher level of transparency in investment rule-making
- Adopting Investor-State Dispute Settlement (ISDS) mechanisms and promoting alternative dispute resolution methods

Liberalization, Protection, Facilitation, and Promotion are the ACIA's four pillars, and to achieve the end goal of the AEC by 2015, its guiding principles include: (i) Achieving a free and open investment environment in the region through progressive investment liberalization and improving the transparency and predictability of investment rules, regulations and procedures conducive to increased investment; (ii) Benefiting domestic and international investors and their investments based in ASEAN and providing enhanced protection to investors and their investments; (iii) Promoting the ASEAN region as a whole as an integrated investment area that has favourable conditions for domestic and international investment; (iv) Maintaining and according preferential treatment among Member States with no back-tracking of commitments made under previous agreements; (v) Granting special and differential treatment and other flexibilities to Member States including reciprocal treatment in the enjoyment of concessions amongst them; and (vi) Openness to expand the scope of the ACIA to cover other sectors in the future.

The ACIA covers almost all forms of investment (excluding only the reservations made by members in the ACIA schedule of reservations), with liberalization provisions



covering the five main sectors of manufacturing, agriculture, fishery, forestry, mining and quarrying, as well as services incidental to these sectors. Liberalization is expected to progress steadily towards 2015, as member states gradually phase out their reservations regarding investments in certain industries.

## **2.1. Investment Eligible for the ACIA Implementation**

In order to benefit from the ACIA, investment must be made by either a natural person (national, citizen, or permanent resident) of any ASEAN country or by an ASEAN-based juridical person that fulfills the requirements laid down in the ACIA.

In order for an investment by a non-ASEAN party to be protected under the ACIA the following conditions must be fulfilled:

- The investment is made by a juridical person in an ASEAN member state. The juridical person may be any legal entity defined as such by the relevant member country.
- The non-ASEAN party must own or control (i.e. have power to name a majority of its directors or legally direct the actions of) the ASEAN legal entity.
- The juridical person must carry out substantial business operations in the ASEAN member state in which it was first established.
- The non-ASEAN third party is from a country with diplomatic relations with the relevant ASEAN member state.

## **2.2. Benefits of ACIA to ASEAN Investors**

Benefits derived from ACIA include investment liberalization, non-discrimination, transparency, investor protections, and Investor-State Dispute Settlement.

### ***2.2.1. Investment Liberalization***

The Agreement liberalizes cross border investment in five sectors: manufacturing, agriculture, fishery, forestry, mining and quarrying, and the services incidental to each. Each ASEAN member state submitted a list of reservations for these sectors, and anything not on the list is subject to national policy, liberalized and open to ASEAN investors.

Each member state is then responsible to reduce or eliminate their reservation list in accordance with the three phases of the Strategic Schedule of the AEC Blueprint (2008-2010, 2011-2013 and 2014-2015).

ASEAN countries are also committed to enhancing cooperation in areas including: investment policy convergence; procedures for investment applications and approvals; information exchange on investment related, rules, regulations, policies and procedures; enhanced coordination among government ministries and agencies; a higher level of consultation with private sector stakeholders to facilitate investment.

To help promote the ASEAN region as an integrated investment area that has favourable conditions for domestic and international investment, all member states agree through the ACIA to: (i) create the necessary environment to promote all forms of investment and new growth areas in ASEAN; (ii) Promote intra-ASEAN investment, particularly investments from ASEAN-6 (Brunei, Indonesia, Malaysia, the Philippines, Singapore and Thailand) into the less developed ASEAN countries; (iii) Nurture the growth and development of small and medium enterprises; and (iv) Promote joint investment initiatives focusing on regional clusters and production networks.

### ***2.2.2. Non-Discrimination***

Equality in treatment for ASEAN investors and their investments is another important feature of the ACIA. The National Treatment (NT) and Most-Favoured-Nation (MFN) Treatment principles of the agreement obligate the ASEAN member states to not discriminate and treat ASEAN investors less favourably than either local or foreign competitors. Under NT, an ASEAN country agrees to treat investors from any ASEAN country no less favourably than it would treat its investors in the admission, establishment, acquisition, expansion, management, conduct, operation and sale or other disposition of investments in its territory. Under MFN Treatment, all ASEAN investors must be treated equally and this includes investors from non-ASEAN countries. In addition, member states cannot impose any specific nationality requirements on senior management unless there is an official published reservation, and if a member state requires the board of directors in a foreign company to be of a particular nationality or be residents, it cannot impair the ability of the investor to control its investment. The ACIA also guarantees no performance requirements and cannot impose conditions like minimum local contents, export requirements, or trade balancing requirements.

### ***2.2.3. Transparency***

Another of the ACIA's guiding principles is to improve the transparency and predictability of investment rules, regulations and procedures conducive to increased investment. To show that the ACIA is rule-based and promotes predictable investment rules, transparency is reflected in many provisions.

### ***2.2.4. Investor Protections***

The ACIA entitles eligible investments to a number of protections. Most of these protections oblige the host state of such investments to provide compensation should it fails to uphold its obligations to a free and competitive investment environment.

#### *Fair and equitable treatment*

The government of any host country must abide by its laws and regulations when exercising its power, and is not allowed to make arbitrary decisions. In the event that legal action is taken against any investor, the investor will be given the right to defend itself,

with access to legal representatives and opportunity to appeal any adverse outcomes or decision.

#### *Full protection and security*

The host government is obliged to provide protection and security to all investments in the event of physical danger (for instance during riots or demonstrations). In the event of losses suffered as a result of armed conflict, strife or similar events, host countries must compensate the affected investors on a non-discriminatory basis.

#### *No unlawful expropriation*

Any ASEAN state which expropriates any ACIA protected investment, directly or indirectly, is obliged to provide adequate and effective compensation to the affected investors in a prompt fashion in due accordance with law. Compensation must be fully realizable and transferable between ASEAN member states and equivalent to the fair market value at the time the expropriation was announced or occurred. Expropriation is only allowed when undertaken for public purposes and when it is done in a non-discriminatory manner.

Exceptions to this include when expropriation is allowed to acquire land subject to the investment, provided compensation is paid to the investor in accordance with domestic laws, and when host states may impose a compulsory license for intellectual property in accordance with domestic law.

#### *Free transfer of funds*

Any investor may freely and without delay conduct investment-related transfers in and out of the territory of the ASEAN state in which it has invested. These transfers may be made in freely usable currencies and at the market rate of exchange at the time of transfer. In exceptional circumstances this right may be limited through good-faith application of the host country's laws and procedures, for instance with regards to bankruptcy, insolvency, trading in securities and futures, taxation, and severance for employees.

In limited circumstances, capital transactions may also be restricted on a general basis if requested by the International Monetary Fund (IMF), as a measure to safeguard the balance of payments, or when capital movements threaten to cause serious economical or financial disturbance in the host country.

#### *Protecting insurers' right to recover*

If an insurer has covered the lawful obligations of a host state to the investor, the insurer has the subrogated right to compensation from the host state.

### ***2.2.5. Investor-State Dispute Settlement***

Another valuable component of the ACIA is its Investor-State Dispute Settlement (ISDS) mechanisms and the promotion of alternative dispute resolution methods. ASEAN investors can resolve disputes by using domestic courts and tribunals, through international

arbitration including ICSID, UNCITRAL, and other agreed rules, and by means of alternative dispute methods: mediation, conciliation, and consultation & negotiation. A disputing investor must show that it incurred a loss or damage by reason of or arising out of the breach of the host ASEAN member state of its obligations under ACIA relating to the management, conduct, operation or sale or other disposition of a covered investment. For any disagreements about ACIA interpretation other than investment disputes, all parties must use the existing ASEAN State-to-State dispute settlement mechanism under the ASEAN Protocol on Enhanced Dispute Settlement Mechanism.

### **2.3. Vietnam's Reservation List under the ACIA**

No investment licenses shall be issued to foreign investors in the following sectors in Vietnam:

- Production of firecrackers including fireworks and sky lanterns or explosive materials; all publishing products and printing - books, brochures, musical books, newspapers, journals and periodicals, recorded media; cigarettes and cigars, alcoholic beverages and soft drinks, and tobacco production; construction glasses, clay bricks, vertical shaft cement production equipment, and baked earth bricks and tiles; fluorescent tubes and bulbs; 10000 DWT cargo ships; under 800 TEU container ships; lighters and under 500 seats passenger ships; cane sugar;
- Cultivating, producing or processing rare or precious plants, breeding or husbandry of precious or rare wild animal and processing of those plants or animals (including both living animals and processed matter taken from animals);
- Services relating to: producing of industrial gas such as oxy, nitro, CO<sub>2</sub> (solid or liquid) caustic soda NaOH (liquid), common used insecticides, and common used paints; dairy processing, cane sugar production, beer and beverage processing, tobacco products;
- Fresh-water fishing, marine fishing, coral and natural pearl exploitation and services related to production of fishing net and twine for fishery, repairing and maintaining of fishing boats, exploiting fresh-water fisheries, and quality control of aquaculture and processing products;
- Mining and quarrying: services related to the application of science and technology to production or services related to testing, adjusting, repairing and maintaining industrial measure and control equipment for oil and gas sector; oil and gas warehouse and supply base services; catering and allied services including food and foodstuff, clean water and vegetable to off-shore construction facilities; manpower supply services including professional manpower, skills and foreign language training for manpower supplied to foreign countries, signing manpower supply contracts with foreign companies;

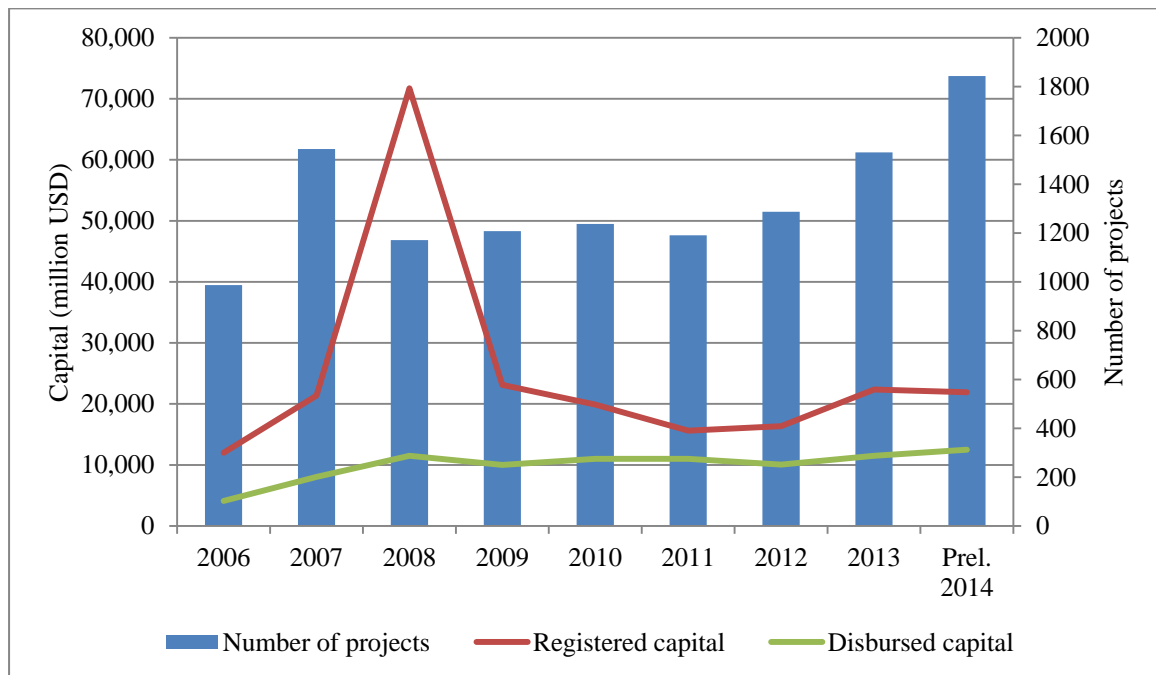
services related to gas processing; services related to geological and exploration drilling; risk assessment, including field-survey, data collection, using special software on impact assessment of frequency and sensitiveness, proposing mitigation measures; services on environment protection and management.

### 3. OVERVIEW OF FOREIGN DIRECT INVESTMENT IN VIETNAM DURING THE PERIOD 2006-2014

#### 3.1. Overview of FDI in Vietnam

FDI has always been an important source of capital in Vietnam. A prospect of a more favourable business environment in the post-WTO period has been a strong incentive to attract FDI to Vietnam. Registered FDI nearly tripled, rising from 21.3 billion USD in 2007 to 71.7 billion USD in 2008. But the global financial crisis dampened the FDI flows to Vietnam. Some recovery has been observed, but not to the 2008 level. On the other hand, although total registered FDI has declined considerably, disbursed capital fell only moderately in 2009 and 2011. This may be the result of several factors: (i) the commitments of the foreign investors have been stronger; (ii) their financial capacity has been improved as the world went out of the global financial crisis.

**Figure 1. FDI in Vietnam during the Period 2006-2014 (million USD)**



Source: GSO data.

#### 3.2. FDI by Sector

Among the five sectors in consideration, manufacturing FDI is dominant, responsible for 56-58 percent of the total during the pre-crisis period 2006-2008. It has been affected strongly during and the financial crisis 2009-2010, where the figure dropped

substantially by half to about 30 percent because of the global capital scarcity and weak export demand on manufacturing. FDI in manufacturing bounced back during the period of the ACIA implementation, reaching record high at 76.8 percent in 2014.

**Table 1. Structure of FDI by Sector, 2006-2014 (percent of registered capital)**

Sector	2006	2007	2008	2009	2010	2011	2012	2013	2014
Agriculture	0.4	0.3	0.5	0.5	0.0	0.2	0.2	0.2	0.1
Forestry	0.2	0.0	0.2	0.1	0.0	0.2	0.0	0.0	0.0
Fisheries	0.1	0.3	0.1	0.2	0.0	0.3	0.3	0.3	0.3
Mining	0.6	1.3	0.2	3.3	0.0	0.6	1.6	0.3	0.0
Manufacturing	58.0	56.4	58.3	31.1	29.6	47.1	61.1	67.4	76.8
Others	40.8	41.7	40.8	64.8	70.4	51.7	36.8	31.9	22.8
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>

Source: FIA data.

The other four sectors subject to ACIA preferential treatment (Agriculture, Forestry, Fisheries and Mining) account for negligible shares of the total FDI. Very few FDI projects were implemented in Forestry during the pre-ACIA period, and there has been no project at all in the period of ACIA implementation.

### 3.3. FDI from ASEAN

Since the Vietnamese economy has been opened to foreign investors, ASEAN has always been among the largest foreign investors in Vietnam (Table 2). The proportion of ASEAN investment in total FDI in Vietnam in several years is even higher than other major investors such as Japan, South Korea and Taiwan. Its share jumped from just 9.5 percent in 2005 to 43.6 percent in 2008, becoming the largest investor.

**Table 2. Structure of FDI to Vietnam, 2005-2014 (percent)**

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>
ASEAN	9.5	8.1	19.6	43.6	5.6	26.8	19.6	15.0	23.1	17.5
Japan	13.8	12.4	6.5	11.8	3.1	12.1	16.8	34.2	26.3	10.1
China	1.8	3.3	2.7	0.6	1.6	3.4	4.9	2.3	10.5	2.1
USA	4.9	6.8	1.8	2.4	43.0	9.7	1.9	1.0	0.6	1.3
Taiwan	11.0	7.0	11.7	13.8	7.0	7.3	3.7	16.3	2.9	5.8
South Korea	13.6	25.9	25.3	0.0	8.3	12.8	9.9	7.9	20.0	36.2
ROW	45.4	36.4	32.4	27.7	31.3	27.9	43.2	23.4	16.7	26.9

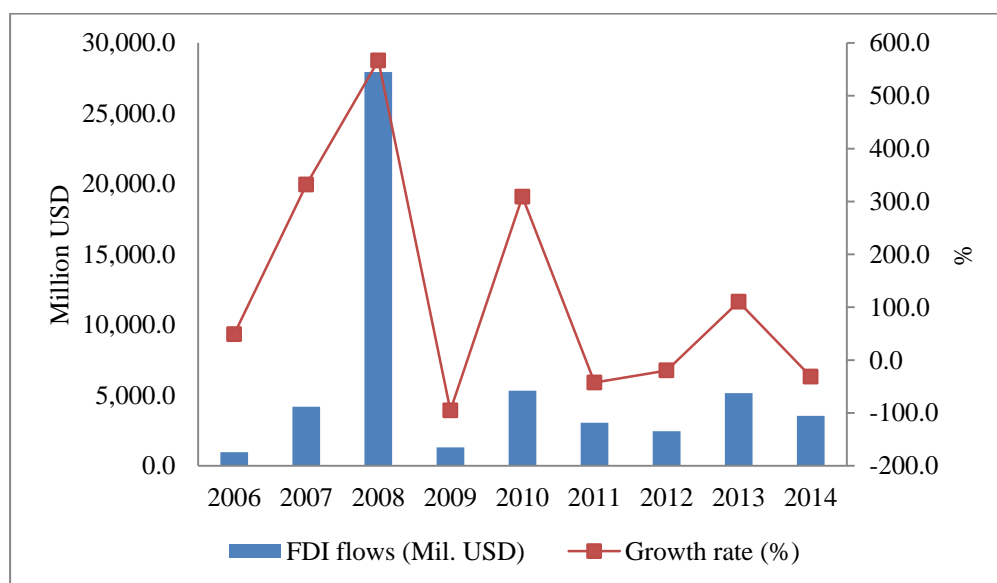
Source: GSO.

Similar to other investors, ASEAN investors have been driven by incentives and preferences offered by Vietnam. The FDI flows from ASEAN have experienced significant changes. The recorded high level of FDI from ASEAN nations was witnessed in 2008, stood at 27,934.8 million USD, which is 42.9 times higher than that of 2005 (651.9 million USD), and attaining the historically highest growth rate of 250 percent per annum during the period of 2005-2008. This growth rate is significantly higher than the overall FDI

growth rate in Vietnam and the ones from other major investors. Specifically, overall FDI grew at the rate of 110.7 percent per annum, that from Taiwan is 127.4 percent, Japan is 100.1 percent, the US is 65.8 percent, and China is 45.7 percent.

FDI flows from ASEAN to Vietnam, nevertheless, dropped sharply in 2009 down to only 1,302.1 million USD, decreasing by 95.3 percent compared to the previous year (Figure 2). This is the largest drop among major foreign investors in Vietnam<sup>1</sup>. In 2010, while the overall FDI to Vietnam followed the declining trend till 2011, FDI from ASEAN went to the opposite direction, increased by 3.1 times in relation to that in 2009, attaining 5,326.0 million USD.

**Figure 2. FDI from ASEAN: Capital Flows and Growth Rate, 2006-2014**



Source: GSO.

During the period of 2011-2012, FDI from ASEAN continued to decline, went down by 42.6 percent and 19.7 percent, respectively, attaining only 2,455.6 million USD in 2012, the second smallest since 2007. The situation only improved in 2013 as the FDI capital flows from ASEAN to Vietnam expanded by 110.2 percent (5,161.4 million USD) before deteriorated again in 2014 (decreased by 31.4 percent to only 3,542.1 million USD).

#### 4. IMPACTS OF ACIA ON INVESTMENT AND SPILLOVER OF POST-ACIA FDI INFLOWS

##### 4.1. Impacts of ACIA on Investment of the Whole Economy

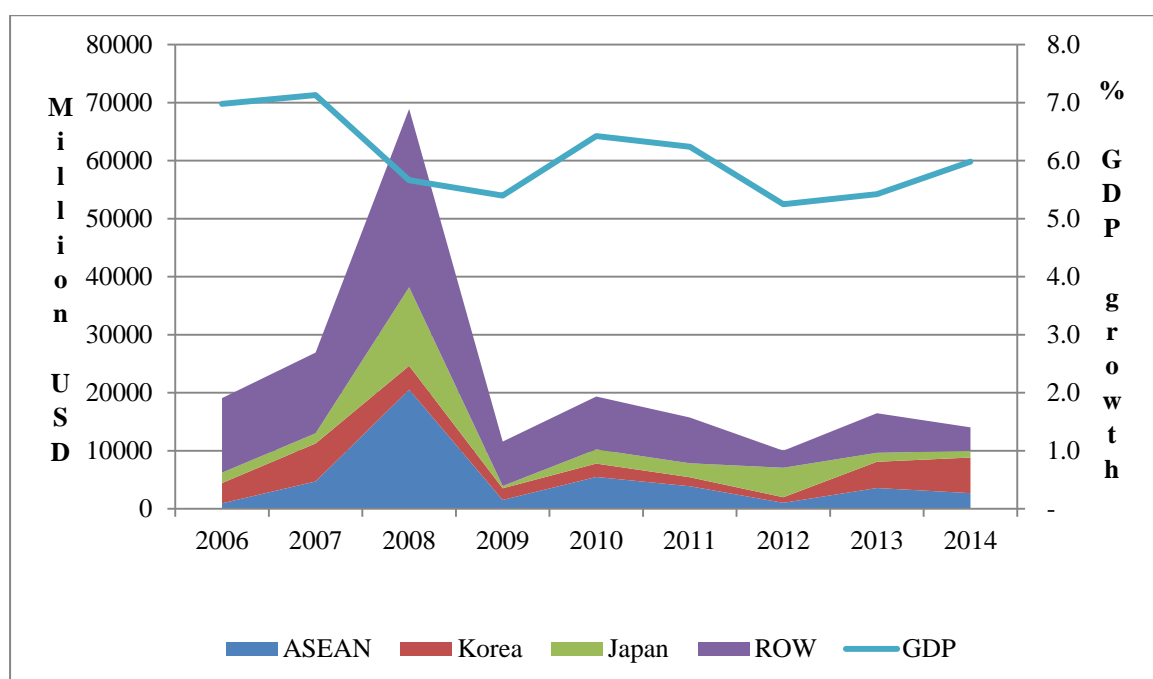
###### 4.1.1. Impacts of ACIA on FDI

In term of registered capital, Figure 3 provides a preliminary picture about the overall impact of the ACIA on FDI. *The ACIA implementation appears to have an*

<sup>1</sup> Overall FDI dropped by 63.9%, Japan - by 90.6%, South Korea - by 81.6%.

*invisible influence on FDI flows from all countries and from ASEAN.* During the period of the ACIA implementation 2012-2014, no apparent rise in FDI in general and from ASEAN in particular can be observed. The total registered FDI (10.02 billion USD) in 2012 (the first year of the ACIA implementation) is the lowest during the period 2006-2014, even lower than the 2009 level (11.59 billion USD) when FDI flows dropped due to the global financial crisis. The FDI flows from ASEAN followed a similar pattern: the registered capital in 2012 was the lowest since 2009 (1,032 vs. 1,523 million USD); only in 2013, the second year of the ACIA implementation, it surged to 3,584 million USD, but still lower than most of the pre-ACIA years (2007-2008, 2010-2011); the flows went down again in 2014 to 2,699 million USD.

**Figure 3. FDI Registered Capital (million USD) by Major Partner and Vietnam's GDP Growth (percent)**



*Source: Authors' calculations using FIA and GSO data.*

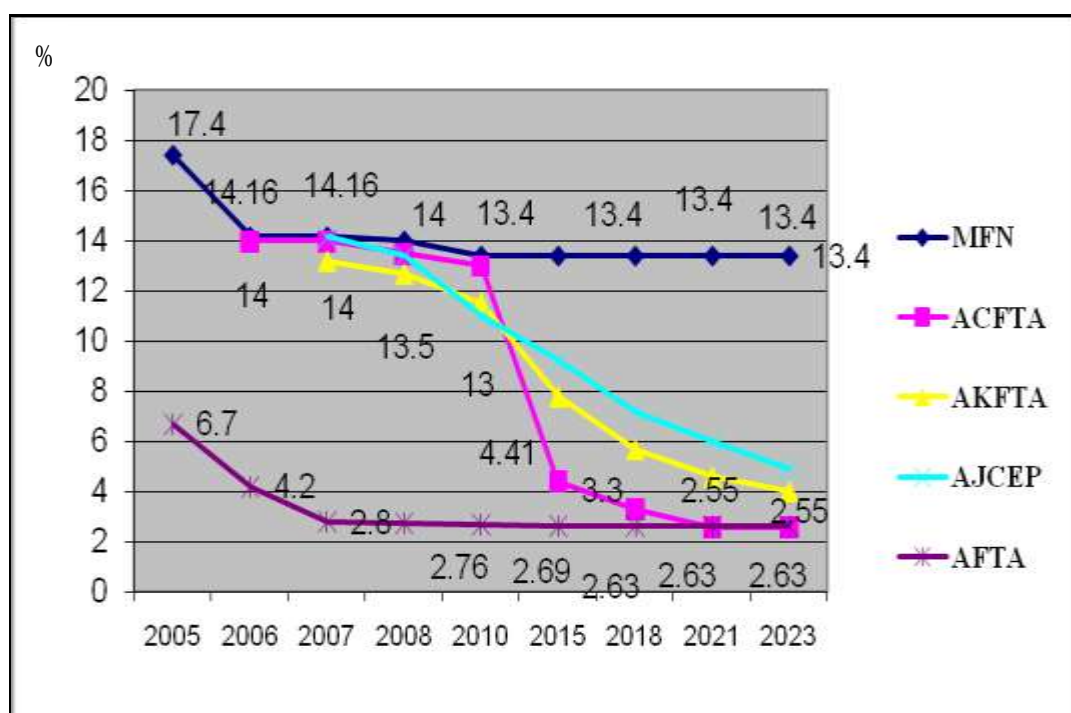
FDI from ASEAN took the downward trend with a more significant drop during the ACIA implementation 2012-2014 compared with other major investors such as Japan and South Korea. ACIA appeared to have smaller impacts than arrangements with some other major partners. ASEAN's investors seemed not to have taken advantage of the ACIA to expand their activities in Vietnam. It is obvious from Figure 3 that VJEPA, which took effect since late 2009, appears to have a considerably higher impact on FDI flows from Japan than the ACIA. The flows increased gradually, and in 2012 they already surpassed those from ASEAN. For South Korea, the FDI flows have exceeded the ASEAN flows since 2013.

One of the explanations may be found from the traditional objectives of FDI, including diversification of risks; taking advantage of the relatively cheap production factors (including host economy's incentives); a relatively large size of the economy as an attractive potential market; and last but not least, a means to penetrate a market (when



existing tariff and non-tariff barriers can be sufficiently restrictive). By 2012, the average tariff on ASEAN imports already went down to below 3 percent (Figure 4). ASEAN investors had very little incentives to invest in Vietnamese market if their primarily objective is avoiding a high tariff barrier. Instead, they could export their ready-made products to Vietnam at a negligible tariff rate. A similar argument is applicable for foreign non-ASEAN investors, who are facing significant trade barriers. Now they can operate their factories in the rest of ASEAN (selected members of which offer very generous concessions, and probably a more favourable investment environment) to export to Vietnam.

**Figure 4. Tariff Reduction Roadmap by Major FTAs in Vietnam (%)**



Another explanation to the ACIA vague impacts on FDI inflows come from weak dissemination of preferential treatment under ACIA to potential investors. A large number of foreign investors are not aware of the ACIA and preferential treatments offered by it.

In term of realised capital, growth rates of FDI inflows into Vietnam have been lower than the FDI growth rates to ASEAN during the ACIA implementation period, although Vietnam performed better than the world (Figure 5). This suggests that Vietnam has been a more appealing destination than many other regions, but an underperformer within ASEAN.

This may be due to the fact that the investment environment in Vietnam is not as good as in other ASEAN members despite a range of incentives provided by the ACIA, for instant cumbersome administrative formalities, inadequate infrastructure, a shortage of the human resource, all these result in high production costs and consequently low return.

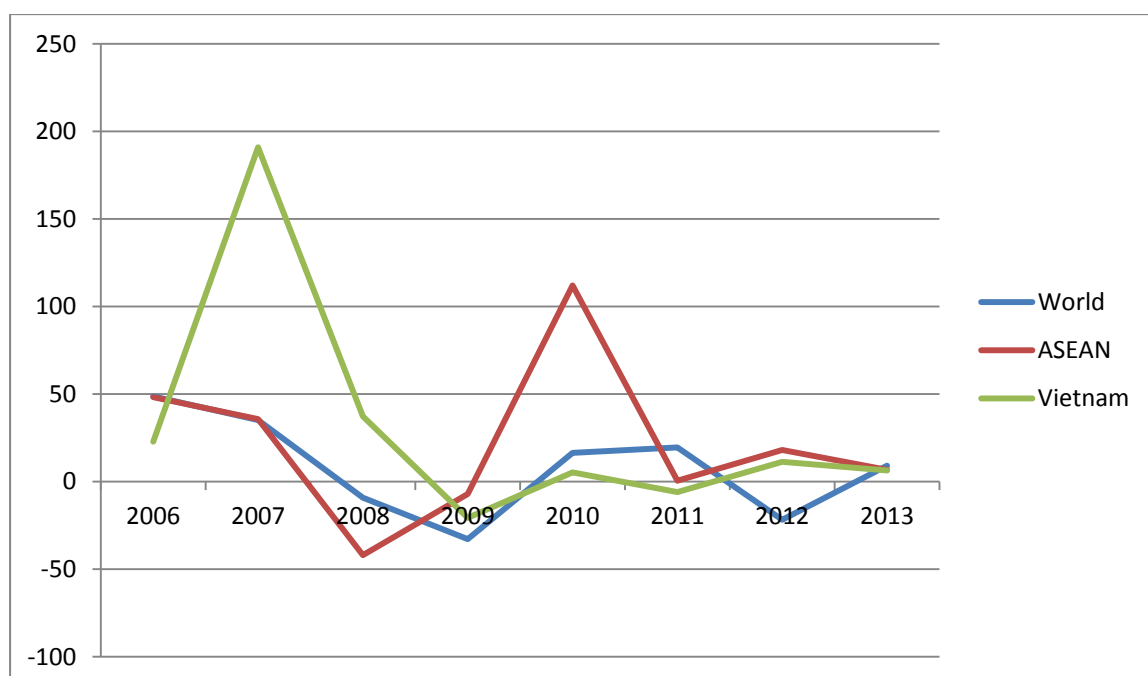
Furthermore, the ACIA impacts might be diminished by other factors, e.g. the difficulties during the post-global financial crisis period. Last but not least, several ASEAN members managed to sign and implement many more FTAs under which foreign investors enjoyed more preferential treatment than in Vietnam.

On the other hand, FTAs that Vietnam signed with other trading partners, such as VJEPA, may reinforce the ACIA impact. This is the case because those ASEAN members, who have not signed a bilateral FTA with Japan, want to get a preferential access to Japanese market. Nevertheless, this impact appears to be smaller than the ones mentioned above.

It should be noticed that joining WTO has a huge positive impact on FDI inflows in general and those from ASEAN in particular. In anticipating a WTO membership, FDI flows have already intensified since 2006, peaking 69 billion USD in 2008. Registered capital of FDI projects from ASEAN had a strong upsurge of nearly five folds in 2007 and more than four folds in 2008. These outcomes suggest that institutional improvement – the most important aspect of the WTO commitments – is the driving factor for attracting FDI.

Furthermore, Figure 3 reveals that FDI (both from the world and ASEAN) since 2009 has moved closely with GDP growth, implying that other things being equal, favourable economic conditions are essential, and may be even more important for FDI flows.

**Figure 5. Annual Growth of Inward FDI Flows 2006-2013 (percent)**



*Source: Compiled by authors using UNTAD online data.*

### 4.1.2. Impacts of ACIA on Domestic Investment

Table 3 suggested that in the pre- and post-ACIA implementation period, **overall FDI has a weak influence on domestic investment**. Realised FDI experienced a reduction in 2012, the first year of ACIA implementation. In contrast, domestic investment (state and non-state), especially state one still grew. In 2013, FDI growth recovered strongly, while the growth of state investment decelerated, and non-state investment growth was moderate. In 2014, non-state investment performed better, but FDI growth was slower.

**Table 3. Annual Growth Rate of Realised Investment by Ownership (percent)**

<i>Year</i>	<i>Non-state</i>	<i>FDI</i>	<i>State</i>
2006	15.4	21.4	9.4
2007	27.7	94.5	4.8
2008	-4.0	35.3	-3.1
2009	28.2	-19.3	22.6
2010	20.1	10.0	-0.7
2011	-0.5	-13.9	-9.2
2012	3.8	-3.9	13.5
2013	5.6	8.8	7.3
Prel. 2014	9.5	6.4	6.0

*Source: compiled by authors using GSO data.*

Furthermore, as discussed in Sub-section 4.1.1, ACIA implementation had an invisible impact on overall FDI inflows, which in turn have very weak correlation with domestic investment. This implies that ACIA had a vague impact on domestic investment.

## 4.2. Impacts of ACIA on Investment in Agriculture, Forestry and Fisheries

### 4.2.1. Impacts of ACIA on FDI

#### Agriculture

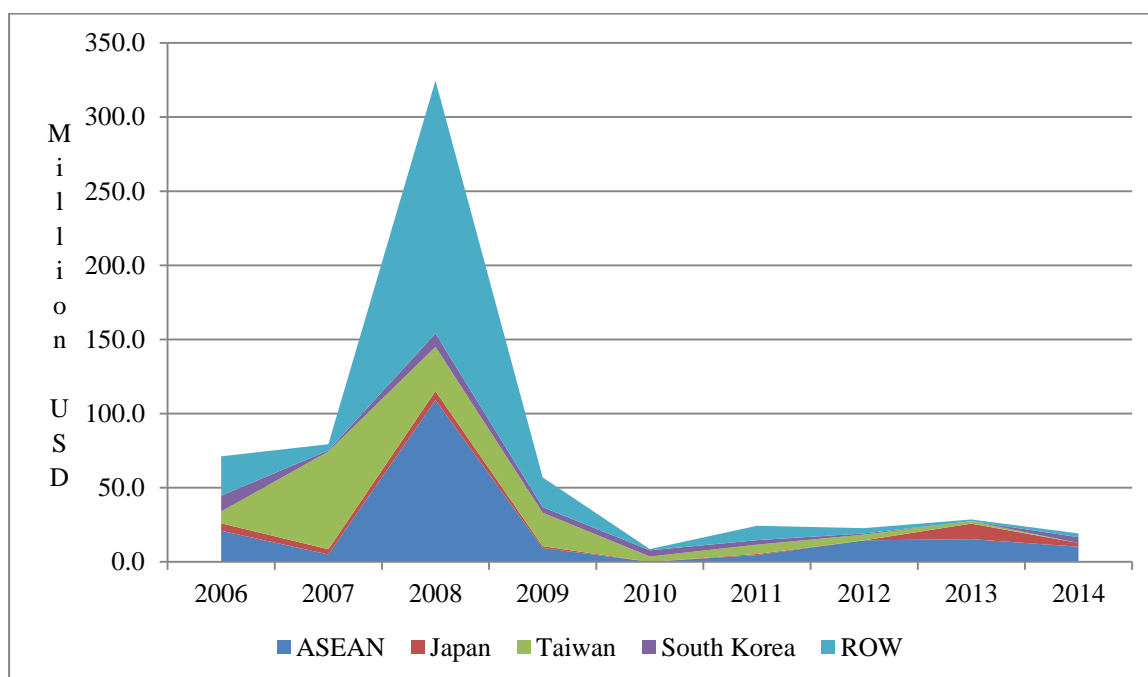
In term of registered FDI, Figure 6 suggests that **ACIA may have some impact on FDI flows from ASEAN in agriculture**. The registered FDI from ASEAN increased considerably from 4.6 million USD in 2011 to 14.5 million USD in 2012 (the first year of the ACIA implementation) and further to 15.3 million USD in 2013, then dropped down slightly to 10.2 million USD. But the ACIA impact is small compared with the WTO accession in 2008, when the registered FDI went up to 109 million USD. During ACIA implementation, ASEAN became the largest foreign investor in agriculture, contributing above half of FDI in the sector.

Figure 6 suggests that the ACIA implementation seems to have no influence on the FDI from the rest of the world into Vietnam, where no noticeable increase is observed.

On the other hand, FDI in agriculture always accounts for a negligible share in total FDI in Vietnam. During the period 2006-2014, the FDI in agriculture accounts for just 0.31 percent of the total FDI flows to Vietnam, with the highest level of 0.49 percent in 2009

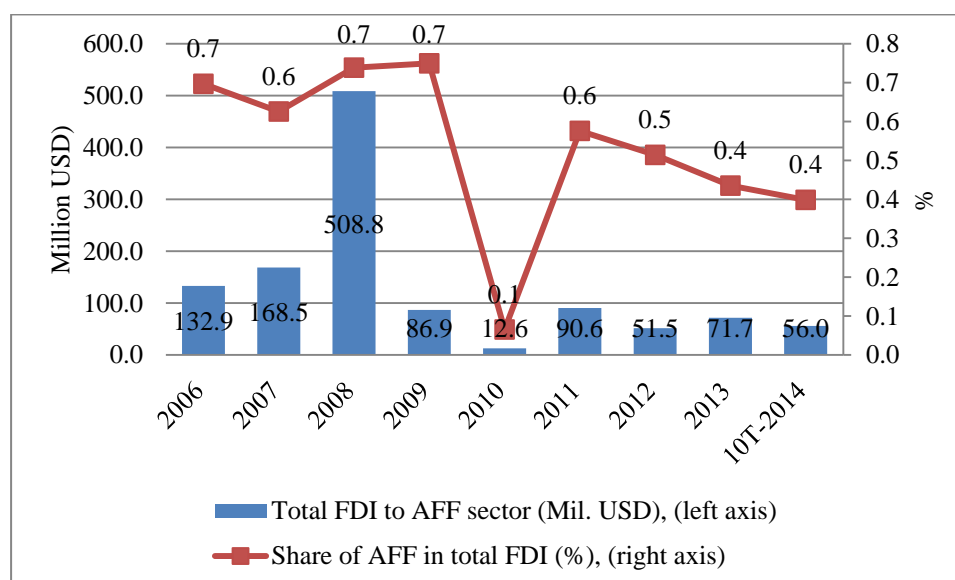
and the lowest level of 0.04 percent in 2010. This implies that economy wide, the ACIA impact on FDI in agriculture is very small.

**Figure 6. FDI Registered Capital in Agriculture by Major Partner (million USD)**



Source: Authors' calculations using FIA data.

**Figure 7. FDI to AFF Sector in Vietnam, 2006-2014**



Source: GSO

### Forestry

*The ACIA implementation had no impact on FDI flows from ASEAN to forestry.* During the period 2012-2014 no registration of any new FDI project from ASEAN or from the rest of the world in forestry has been recorded. In fact, there have been no new FDI

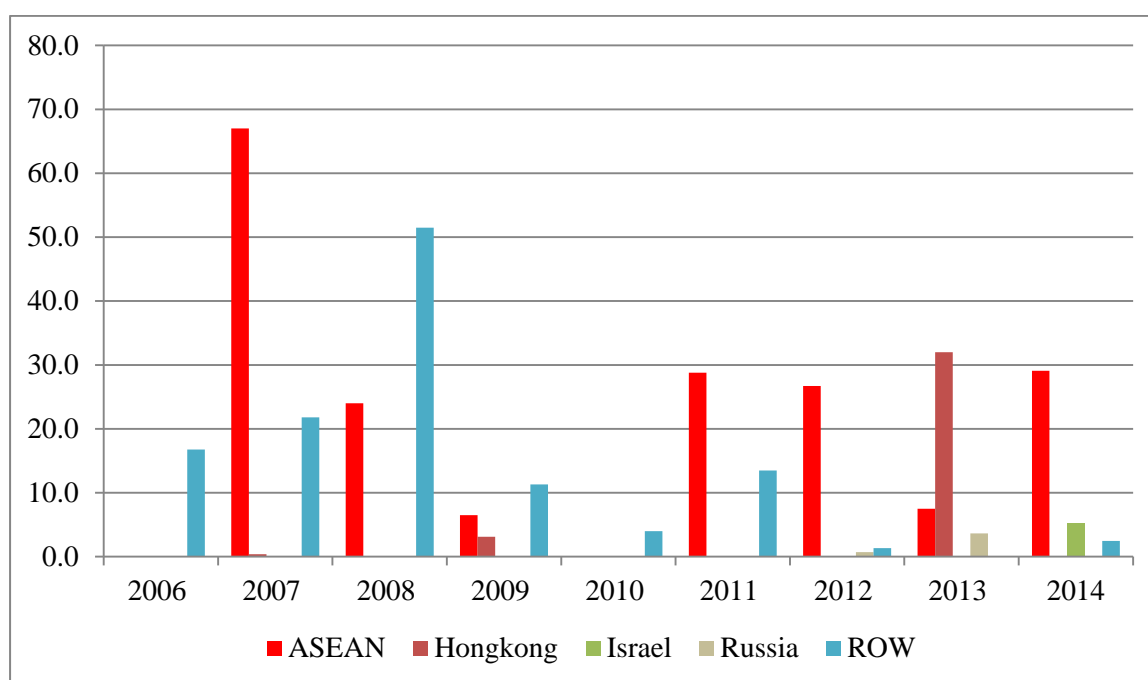
projects from ASEAN in this sector since 2007. Forestry in Vietnam seems to be not very attractive to the ASEAN members due to long repayment period and small comparative advantage.

### Fisheries

In the pre-ACIA period, ASEAN was already often the largest foreign investor in fisheries. ***The ACIA impact on FDI flows from ASEAN is not prominent.*** The level of registered FDI from ASEAN in 2012 is 26.7 million USD, still lower than in 2011, and fell sharply to 7.5 million USD in 2013. In 2014, the registered FDI resumed, but just slightly higher than the level in 2011. The impact of the WTO membership on FDI from ASEAN is substantially higher, reaching 67 million USD in 2007. ACIA seems to have no impact on FDI flows from the rest of the world in fisheries.

Similar with the situation in agriculture, FDI in fisheries makes a tiny share at less than 0.3 percent of the total FDI flows to Vietnam between 2012 and 2014. Hence, the ACIA impact on FDI in fisheries relative to the FDI in the rest of the economy is not large.

**Figure 8. FDI Registered Capital in Fisheries by Major Partner (million USD)**



Source: Authors' calculations using FIA data.

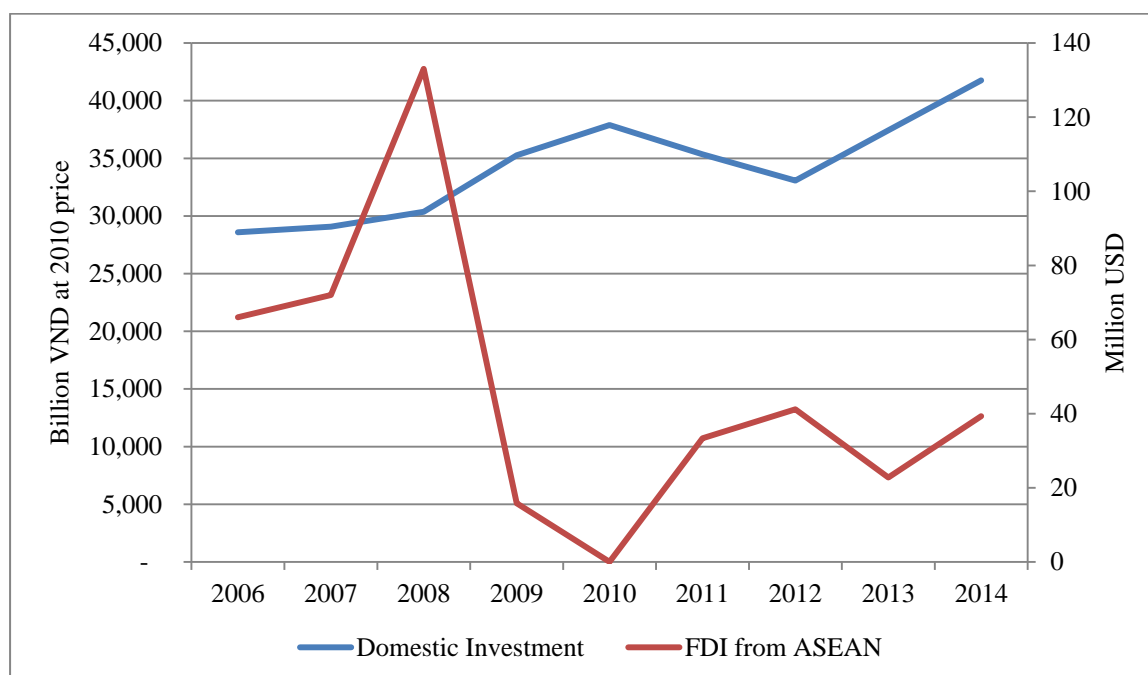
#### ***4.2.2. Impacts of ACIA on Domestic Investment in Agriculture, Forestry and Fisheries***

Due to unavailability of the disaggregated investment data on agriculture, forestry and fisheries, this subsection can only discuss the ACIA impacts on AFF as a whole. Figure 9 shows that ***the ACIA implementation had an unclear impact on domestic (state and non-state) investment in AFF.*** In 2012 (the first year of the ACIA implementation), when FDI from ASEAN increased, realized domestic investment dropped. In 2013 the

situation reversed where the FDI fell to a level lower than that in 2011. Only in 2014 both domestic investment and FDI moved in the same direction. Over time, domestic investment in AFF tends to be more stable than FDI.

In summary, with regard to FDI flows from ASEAN, the ACIA implementation had a small impact in agriculture, unclear impact in fisheries and no impact in forestry. The ACIA implementation has not shown a noticeable impact on both FDI from the rest of the world and domestic investment.

**Figure 9. Domestic Investment (billion VND at 2010 price) and Registered FDI (million USD) from ASEAN in Agriculture, Forestry and Fisheries**



Source: Authors' compilation using GSO and FIA data.

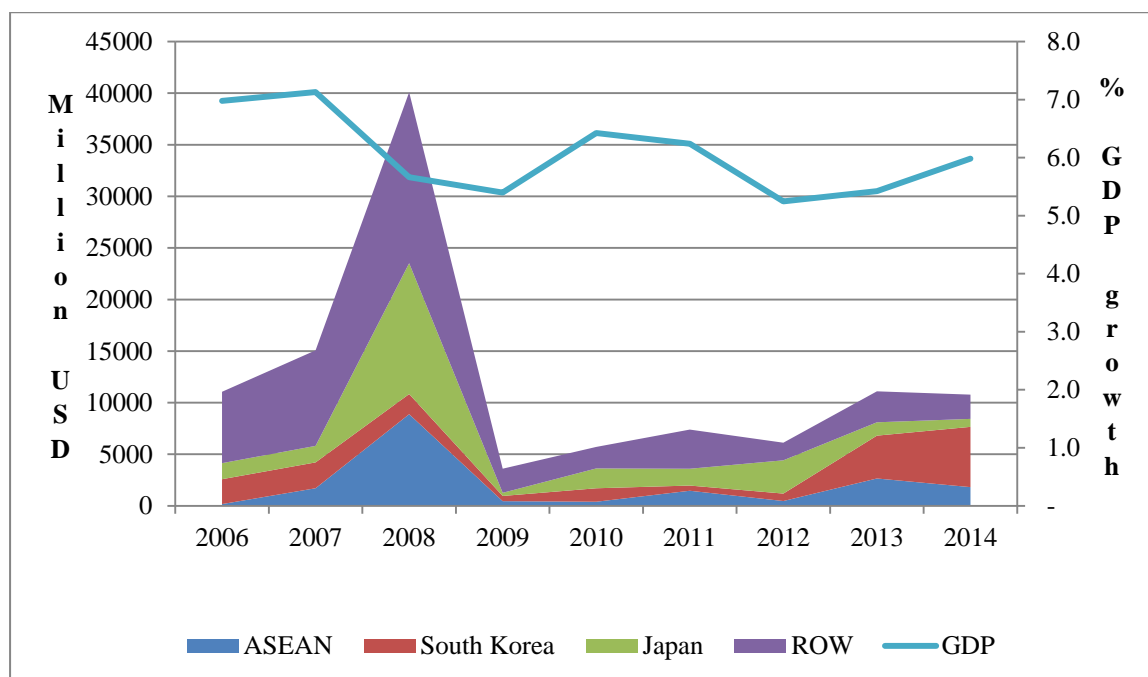
### 4.3. Impacts of ACIA on Investment in Manufacturing

#### 4.3.1. Impacts of ACIA on FDI

*ACIA impact on FDI flows from ASEAN in manufacturing is not very notable.* In 2012, the first year of the ACIA implementation, the registered FDI from ASEAN did not go up to respond to the preferential treatments brought by the ACIA. FDI from ASEAN in manufacturing fell down sharply from 1463.2 million USD in 2011 to 465.7 million USD in 2012. An increase was only observed in 2013, when the registered FDI went up significantly to 2652.1 million USD. In 2014, it declined again down to 1814.4 million USD despite some economic recovery in the region. As demonstrated in Figure 10, this pattern is similar to that of the overall level of FDI from ASEAN, which in most of the years moved together with the GDP growth. This is the case because FDI in manufacturing has often made the largest share in the total FDI, except for the post-crisis years 2009 and 2010. The ACIA impact in manufacturing is much smaller than that of the WTO accession.

There has been a strong surge in registered FDI from South Korea since 2013, but it may be the impact of an intensified economic cooperation between Vietnam and South Korea.

**Figure 10. FDI Registered Capital in Manufacturing by Major Partner (million USD) and Vietnam's GDP Growth (percent)**



Source: Authors' calculations using FIA and GSO data.

#### 4.3.2. Impacts of ACIA on Domestic Investment in Manufacturing

Domestic investment and registered FDI during the period 2006-2014 shows that there is little correlation between domestic investment and FDI in manufacturing. In 2008 and 2011, when domestic investment declined, registered FDI rose. In the remaining years, the movement of these two flows often went to opposite directions. An estimation of the correlation between these two flows gives the value of -0.2, which implies that when registered FDI from ASEAN increased, domestic investment may drop. This may support a finding that *ACIA had no positive impact on domestic investment in manufacturing*. Again, while FDI from ASEAN fluctuated from year to year, domestic investment shows a more stable trend.

#### 4.4. Impacts of ACIA on Investment in Mining

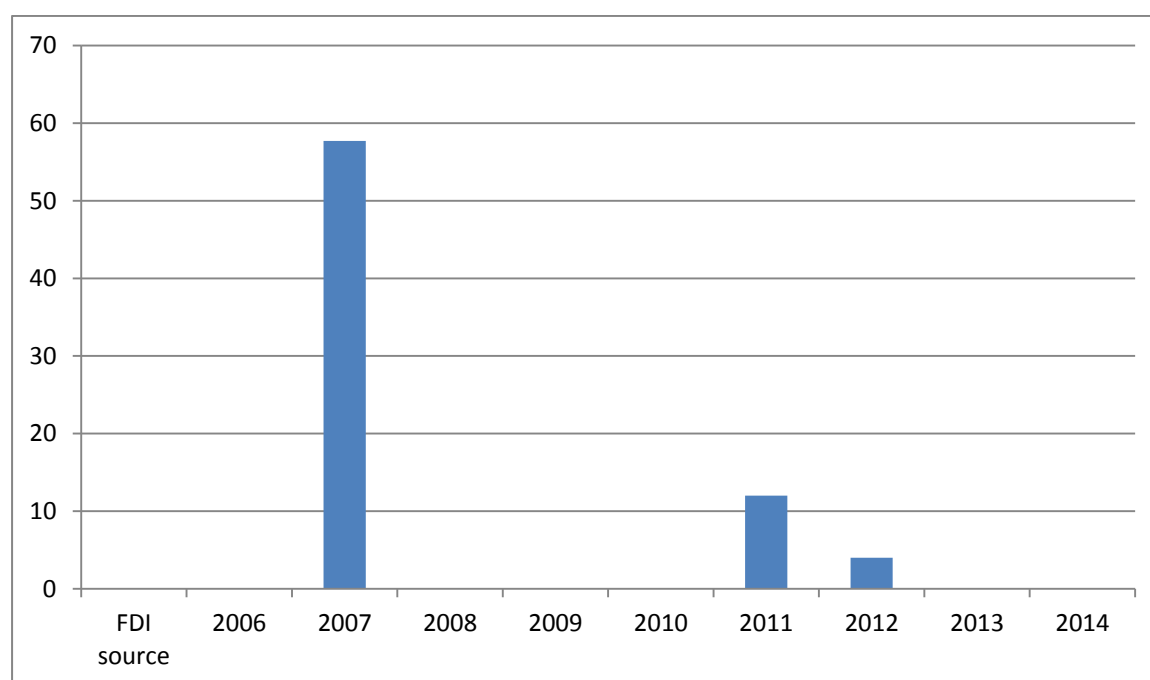
The mining has received a negligible share in total FDI in Vietnam. The number of FDI projects in mining and quarrying was less than 10 projects annually, accounting for nearly 0.4 percent of total FDI projects in Vietnam in the period of 2006-2014. Similarly, the share of registered FDI in this sector in total registered FDI was minor, averaging just nearly 0.9 percent annually.

**Table 4. FDI in Mining in Vietnam**

Year	Total number of FDI projects in mining	Share of FDI projects in mining in total number of projects (%)	Number of ASEAN FDI projects in mining	Registered investment in mining (Mill USD)	Share of FDI in mining in total registered investment (%)	Registered ASEAN FDI in mining (Mill USD)
2006	5	0.5	0	107.60	0.6	0.0
2007	9	0.5	1	345.77	1.3	57.7
2008	7	0.4	0	136.36	0.2	0.0
2009	8	0.7	0	386.35	3.3	0.0
2010	0	0.0	0	0.00	0.0	0.0
2011	5	0.4	1	98.40	0.6	12.0
2012	7	0.5	1	161.93	1.6	4.0
2013	4	0.3	0	42.32	0.3	0.0
2014	0	0.0	0	0.00	0.0	0.0

Source: Author's calculation from FIA database

During the period of 2006-2014, there were only three FDI projects from ASEAN investing into mining industry in Vietnam, with a very small investment share to the total FDI in this sector (see Table 4). This illustrates that mining industry in Vietnam has not been impacted by the implementation of ACIA.

**Figure 11. ASEAN FDI in Mining in Vietnam (Million USD)**

Source: Compiled by authors, using FIA database.

## 5. IMPACTS OF ACIA ON DOMESTIC PRODUCTION

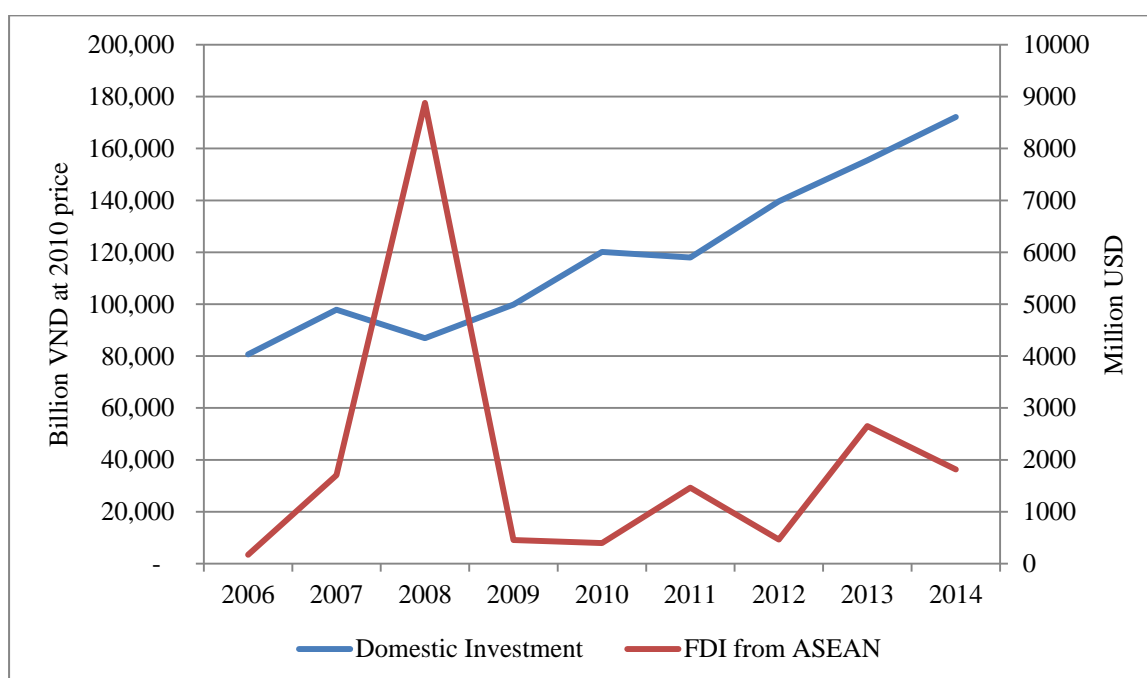
As discussed in Section 4, the ACIA implementation had some impact on FDI from ASEAN in agriculture and manufacturing only. This implies that there was no direct impact on domestic production in the remaining three sectors in consideration (forestry, fisheries and mining).



The ACIA impacts on domestic production may go through the following channels:

- Firstly, increased FDI in the sector in consideration during the construction phase (usually three to five years) results in its higher demand on construction and capital goods, both from domestic and imported sources.
- Secondly, increased FDI in the sector in consideration results in production expansion in the sector in consideration in later years (usually three to five years). Imports of the domestic-substituting goods may go down. Nevertheless, as the ACIA has been implemented since 2012, this type of impact can be considered as zero.

**Figure 12. Domestic Investment (billion VND at 2010 price) and Registered FDI (million USD) from ASEAN in Manufacturing**



Source: GSO and FIA data.

- Thirdly, increased production inputs (from upstream industries) for the sector in consideration result in an expansion of upstream industries. This only happens when the project starts its operation (usually three to five years from the project implementation). As the period of the ACIA implementation is just three years, this impact should be zero.
- Fourthly, expansion of the downstream industries as a result of ACIA leads to increased demand for inputs from the sector in consideration. So far, this impact should also be zero.

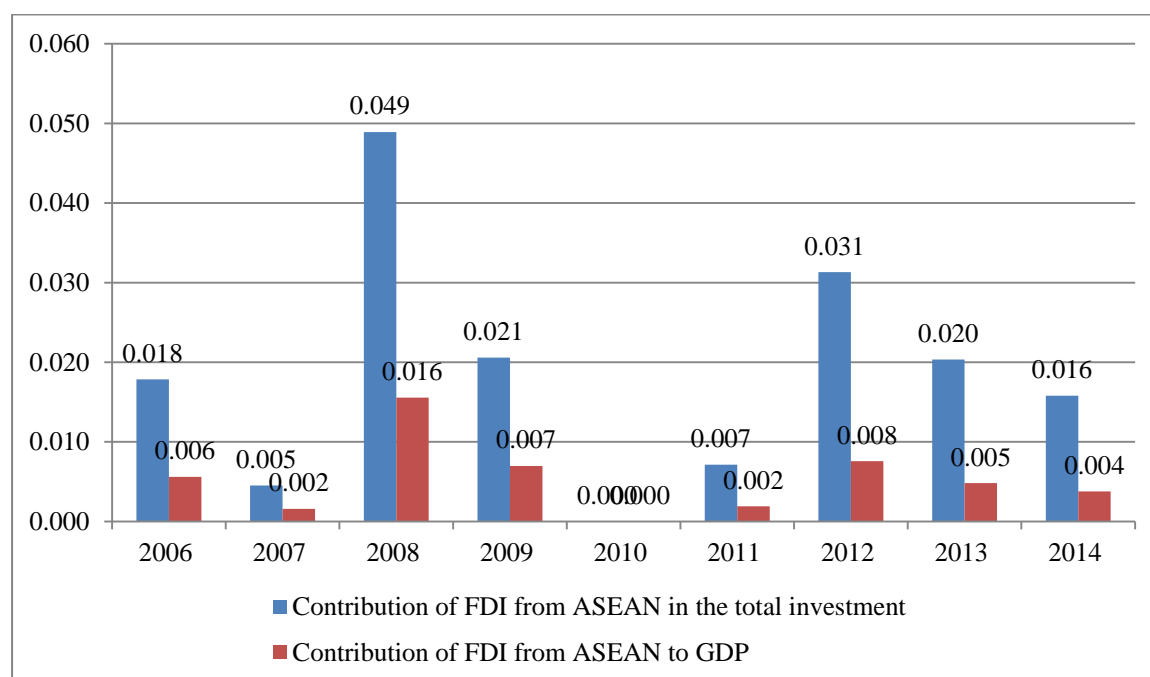
For the above reasons, this section only looks at the impact resulting in a higher demand on construction and capital goods, both from domestic and imported sources. The higher demand on construction and capital goods affects the expenditure side of the GDP through an increased investment in production assets.

Due to the lack of the data on composition of investment goods in the two sectors in consideration, it is assumed that the share of registered FDI from ASEAN in the total investment is a proxy for the share of gross fixed capital formation from ASEAN in the total fixed capital formation.

### 5.1. Impact of FDI from ASEAN in Agriculture on GDP through Building up Production Assets

Contribution of FDI from ASEAN in agriculture to both investment and GDP is very tiny. As can be seen in Figure 13, in the post-ACIA period, the contributions are larger than that in the two years prior to the ACIA implementation (2010 and 2011). This implies that ACIA had some impacts on investment and GDP, but their magnitude is still very modest, just 0.016-0.03 percent of the total investment in the post ACIA years. The contribution on GDP is really too small (0.004-0.008 percent GDP). If other thing being equal, the net impact of the ACIA implementation is the difference between the post- and pre-ACIA period.

**Figure 13. Contribution of FDI from ASEAN in Agriculture to the Total Investment and GDP (percent)**



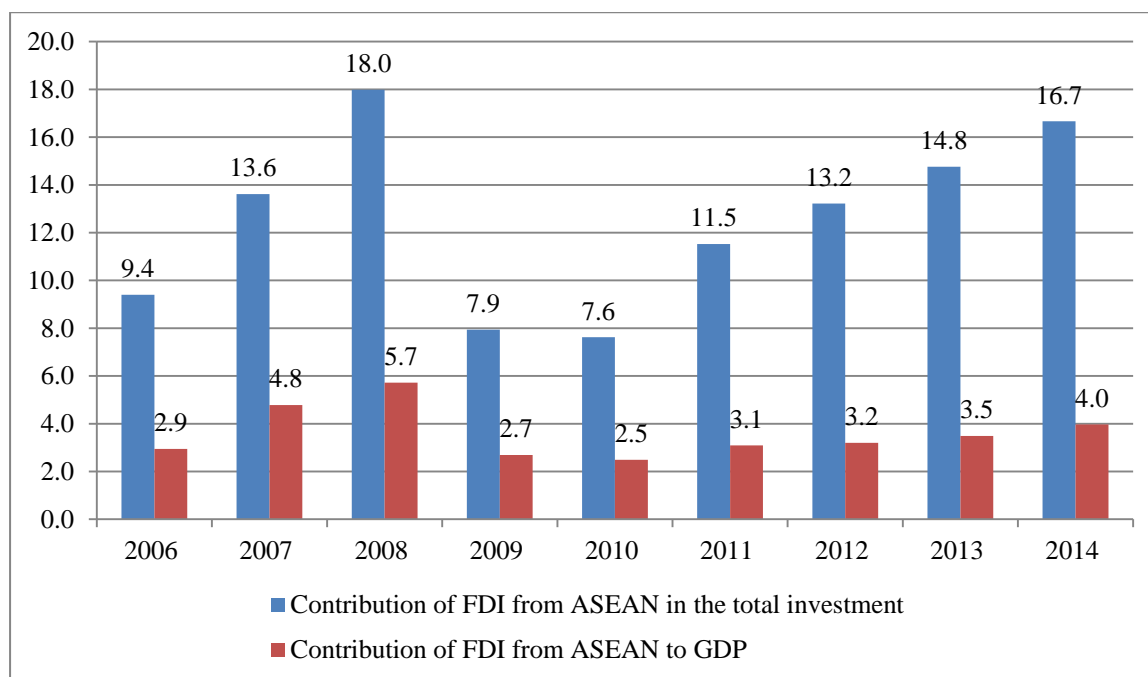
*Source: Authors' calculation using GSO and FIA data.*

### 5.2. Impact of FDI from ASEAN in Manufacturing on Building up Production Assets and GDP

Contribution of FDI from ASEAN in manufacturing to both investment and GDP is much larger than the one in agriculture. FDI from ASEAN in manufacturing contributed 13.2-16.7 percent of the total investment, compared with 7.6-11.5 percent in the pre-ACIA

years. The contributions to GDP are also good, from 3.2 percent to 4 percent of GDP. Again, the net impact of the ACIA implementation is the difference between the post- and pre-ACIA period, which are between 0.1 and 1 percent of the GDP.

**Figure 14. Contribution of FDI from ASEAN in Manufacturing to the Total Investment and GDP (percent)**



*Source: Authors' calculation using GSO and FIA data.*

## 6. IMPACTS OF ACIA ON EXPORTS

As FDI projects from ASEAN have not started their production, no impact on exports can be made.

## 7. IMPACTS OF ACIA ON IMPORTS

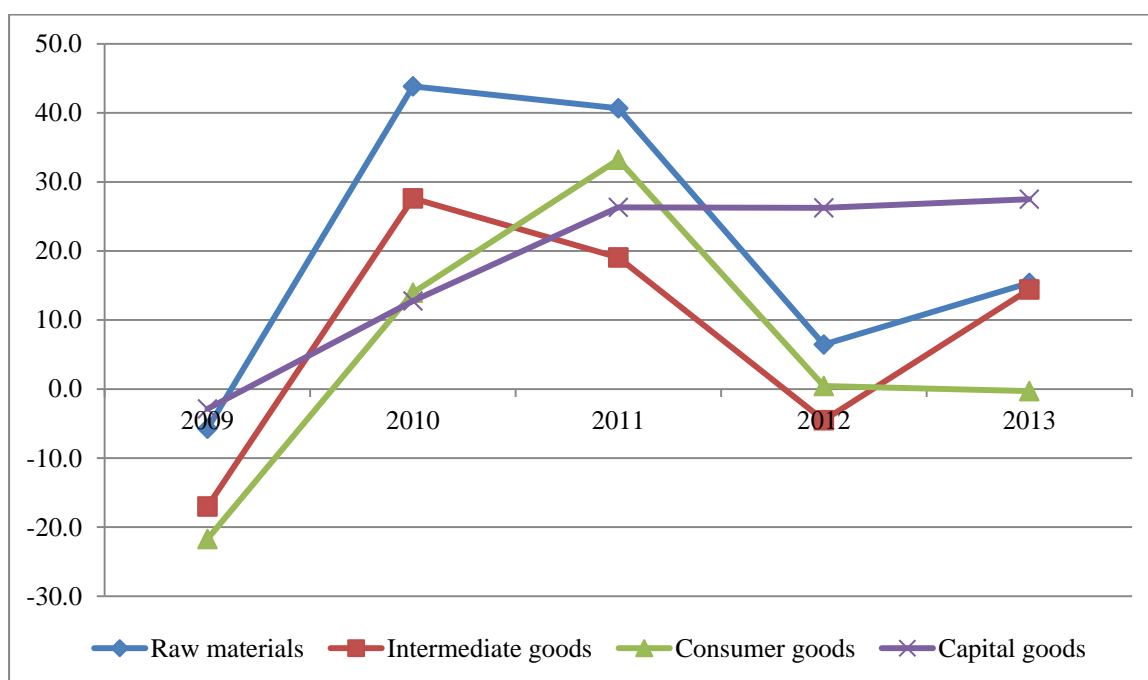
As most of the FDI projects from ASEAN have been in their construction period, impacts that they could make just are those on increased imports of capital goods, while imports of raw materials and intermediate goods (required for production), as well as consumer goods (could possibly substituted by domestic production) are not much affected. Recall that the overall level of registered FDI from ASEAN fell in 2012 and rose slightly in 2013, so any increase of imported capital goods in 2012 could not be attributable to the ACIA implementation.

Figure 15 shows that in 2012 and 2013 imports of capital goods went up with growth rates considerably higher than in previous years (annual average 26.9 percent during 2012-2013 vs. 11.4 percent during 2009-2011). The surge in 2012 would come from FDI projects which received their license during the first years of WTO accession and purchased machines and equipment toward the end of their construction phase, but not yet

those FDI project from ASEAN in the post ACIA period. The higher import value in 2013 could result from the surge in FDI from ASEAN in post-ACIA period, together with those projects from Japan and Korea, as well as domestic investment. Thus, the ACIA implementation appears to have some impact on the imports of capital goods.

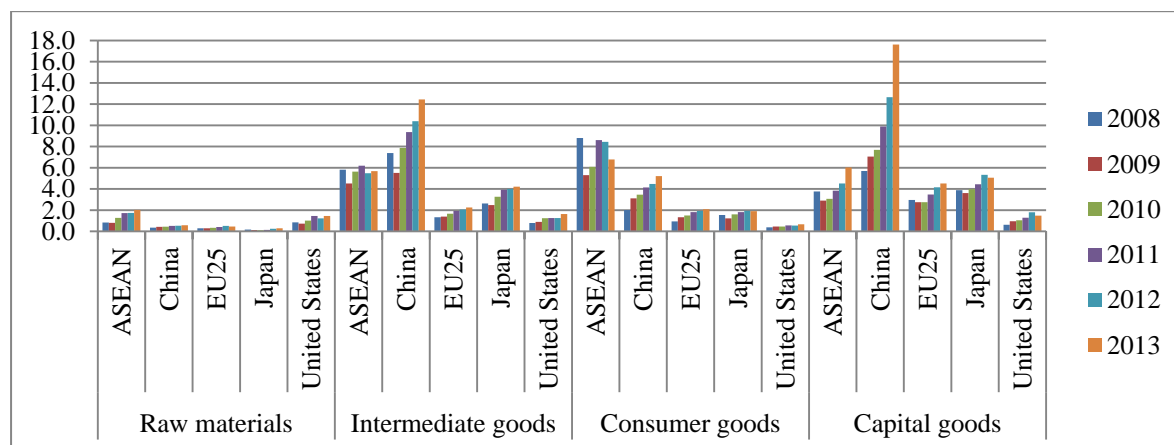
Figure 16 illustrates imports by Vietnam from major trading partners during the period of 2008-2013. As such, ASEAN has been the largest supplier of consumer goods and raw materials for Vietnam, which was not affected by ACIA during its first three years of implementation for the reason mentioned above.

**Figure 15. Annual Growth of Imported Goods by Vietnam by the Broad Economic Categories (percent)**



Source: Compiled by authors using UNCOMTRADE database.

**Figure 16. Imports by Vietnam from Selected Trading Partners, 2008-2013 (Billion USD)**



Source: Compiled by authors using UNCOMTRADE database.

China has been the largest source of Vietnam's imports of capital goods and intermediate goods, with the former increased at a faster pace since 2011. ASEAN, Japan and EU are the next largest suppliers. Increased imports of capital goods, to some extent may result from the start-up of the ASEAN projects during the ACIA implementation. One of the implications of trade and investment liberalization under various FTAs and the ACIA implementation is Vietnam's increasing reliance on imports of capital goods and intermediate inputs from China, which leads to huge bilateral trade deficits borne by Vietnam.

## **8. CONCLUSIONS AND POLICY RECOMMENDATIONS**

### **8.1. Conclusions**

The study finds that the ACIA has modest impacts on attracting FDI from ASEAN and the rest of the world. FDI from ASEAN even took the downward trend with a more significant drop during the ACIA implementation 2012-2014 compared with other major investors such as Japan and South Korea. Growth rates of FDI inflows into Vietnam have been lower than the FDI growth rates to ASEAN during the ACIA implementation period. ACIA also had a vague impact on domestic investment.

By sector, the ACIA implementation had a small impact in agriculture and manufacturing, unclear impact in fisheries and no impact in forestry.

Contribution of FDI from ASEAN in agriculture to both investment and GDP is very tiny. The impact of FDI from ASEAN in manufacturing is larger, between 0.1 and 1 percent of the GDP.

As FDI projects from ASEAN have not started their production, no impact on exports can be made. The ACIA implementation appears to have some impact on the imports of capital goods. Under the implementation of the ACIA and other FTAs, Vietnam's increasing reliance on imports of capital goods and intermediate inputs from China would lead to huge bilateral trade deficits borne by Vietnam.

### **8.2. Recommendations**

The study comes to the following recommendations:

- Current ACIA should be improved to make it more attractive to investors. For instance, the reservation list should be further relaxed, more attractive preferential treatments for ASEAN investors to invest in other member countries (but still need to comply with other national and/or international rules and regulations) would be offered;

- Further measures should be adopted to improve the effectiveness and enforcement of current ACIA, such as strengthening the coordination among ASEAN member countries;
- The preferential treatments provided by the ACIA should be wider disseminated;
- Dissemination of the concessions of FTAs that Vietnam has been or will be involved such as VJEPA, The Vietnam Eurasian Economic Union FTA, TPP, EU) should be improved to attract export-oriented foreign investors;
- The business environment should be further improved to accommodate FDI from the world and from ASEAN in particular.

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