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Regionalisation, Foreign Direct Investment and Poverty Reduction: The Case of ASEAN

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Abstract. This paper examines the impact of foreign direct investment (FDI) on growth and development in the Association of South East Asian Nations (ASEAN). The analysis is based on a research project that interviewed Transnational Corporation (TNC) subsidiaries in Cambodia, Malaysia, Singapore, Thailand and Vietnam. The paper establishes a model on the principal potential impact of FDI on Development, divided into three categories of effect (with many sub-categories): Direct Effects, Multiplier Effects (both consumption and value chain multipliers) and Spillovers. Because ASEAN countries – especially Malaysia, Singapore and Thailand – have been major recipients of FDI for over three decades, TNCs have undoubtedly impacted significantly on growth and development in ASEAN countries. However, it seems that the effects are still primarily due to "direct effects" and the consumption multiplier. The effect through the value chain multiplier is highly variable, probably "middling", while the benefits from spillovers are still someway from being realised across national and regional economies as a whole. By including new member countries of ASEAN in the sample, the paper is able to discuss the benefits and lessons that developing countries can obtain from association with the more experienced countries of the region. More particularly, the paper focuses specifically on lessons for Vietnam in order to ensure a concrete discussion of the issues.

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1. Introduction

Both before and since their entry into the Association of South East Asian Nations (ASEAN) from 1995 onwards, the new member countries of ASEAN (Cambodia, Laos, Myanmar and Vietnam) have looked to their partner member countries for ideas, lessons and inspiration – as well as for direct economic benefits – in order to further their own development, including the central issue of poverty reduction[1]. One of the reasons that these countries joined ASEAN was in order to take part in the great bounty represented by the large-scale influx of Foreign Direct Investment (FDI) into the region during the 1980s and the early part of the 1990s. Since then, partly because of the Asian Economic Crisis, FDI into the region has declined (less so for Vietnam), but the potential benefits of regional cooperation in attracting FDI remain – and for this reason, these countries have played a very full role in the development of the ASEAN Free Trade Area (AFTA) and the ASEAN Investment Area (AIA) (Wee and Mirza 2004).

Perhaps the most conspicuous reason for ASEAN countries to cooperate in promoting inward FDI is associated with the need to enhance individual country and regional competitiveness through cooperation in promoting ASEAN as an investment region – a regional model of attracting FDI. A linked reason is that, because of the region's integration process, it is natural to include investment given that trade arrangements and other aspects of economic cooperation are already part of the region's integration agenda. Clearly investment cooperation is a sub-set of a larger set of regional integration arrangements, but one that can help strengthen the overall integration process. The value of these arrangements, however, depends on the degree to which FDI and Transnational Corporations' (TNCs') regional operation strategies are centred on (or are evolving towards) using combined regional locational advantages (differential levels of resources, human capital, cheap labour and markets in an area of 450 million people) to create value chains across the region (and beyond).[2]

One issue this article seeks to address, an empirical one, is the extent to which these countries have benefited from integration in ASEAN and, in particular, the regional and global value chains established by TNCs. The second issue to be examined is how they can learn from the longer FDI experience of other ASEAN countries in order to ensure maximal net gains from inward FDI. These two issues will be analysed using some of the results of a recent research project conducted by the University of Bradford, “Regionalisation, Foreign Direct Investment and Poverty Reduction: The Case of ASEAN”[3] (“Bradford Study”), one aim of which was specifically to look at the lessons for the newer ASEAN member countries (Cambodia, Laos, Myanmar and Vietnam) emanating from the experience of the older member countries (Brunei, Indonesia, Malaysia, the Philippines, Singapore and Thailand). The next section will describe the research project and provide an analytical framework for the article. The following two sections will look, in turn, at the benefits of ASEAN integration for new member countries and the lessons that these countries can learn from the FDI experience of its neighbours. The final section will conclude with implications and policy recommendations. Since the Bradford Study only included companies from Cambodia and Vietnam in its sample, and because Cambodian sample is small and skewed, the remainder of this paper will use Vietnam as the primary vehicle for understanding the issues outlined above.

2. Analytical Framework and Research Methodology

It is acknowledged in the literature that foreign direct investment (FDI) impacts on the growth and development of host countries (including poverty reduction) in a variety of ways (Giroud, 2003; Klein et al, 2001; UNCTAD, 1999 and 2001), ranging from "direct effects" on employment and training, through classical "multiplier effects" (e.g. workers use their wages to buy goods which stimulates other industries) to "spillover" effects whereby indigenous firms acquire knowledge and technology from foreign firms through a variety of transmission mechanisms. The bones of this perspective, which provides the principal theoretical underpinning for the "Bradford Study", are fairly straightforward (although the operationalisation of the relevant issues is not).

First of all, in any host country, FDI manifests itself in the form of a TNC establishing local operations, usually through one or more subsidiaries (that is enterprises established as legally local entities). These subsidiaries must set-up shop by building a factory and related facilities, buy necessary equipment and supplies and, most importantly, hire workers who will frequently need to be trained-up. These interfaces between the subsidiary company and the economy are typical of the main *direct effects* that FDI has on the host country. The extent of these direct effects depends on the scale of the initial FDI; the technology employed; the numbers of people employed and the training, wages offered; the degree to which the firm can procure essential goods and services (e.g. machinery, construction engineers) locally; and the proportion of profits reinvested periodically in the subsidiary (or other local expansion).

Secondly, since the subsidiary company is a constituent element of the TNC, it is a part of a value chain, both within the country and internationally. These links are both backwards (with suppliers) and forwards (with distributors and sales organisations). Inasmuch as these linkages stimulate activity, employment etc. in supplier and distributor firms and organisations in the host country, then the initial FDI has a multiplier – i.e. amplified – effect beyond the initial direct effect on the local economy. This multiplier can be referred to as the *"value chain multiplier effect"* since it operates along the value chain (i.e. by increasing the output of suppliers and sales organisations) and its extent depends on similar factors to the direct effect. In particular, the multiplier will be effected by the degree to which the value chain linkages are in the host country or without – the greater the proportion of linkages with firms outside the host economy, i.e. in the regional or international domain, the lower will the multiplier effect in the host. (Additionally, it is possible that some local linkages will be with the subsidiaries of other TNCs and this will also dilute the multiplier effect because many such companies will also have some of their linkages abroad.) In addition to the value chain multiplier, there is also a *consumption multiplier effect*: e.g. the subsidiary and its linked firms all pay taxes and their workers purchase goods and services (and pay taxes), all of which results in a boost to other sectors of the economy.

Finally, the subsidiary plays a role in transferring, encouraging or obliging the transfer/take-up of knowledge, technology and skills – in a myriad of forms – to other organisations in the host country, principally through training, demonstration and competitive effects. Collectively this is known as the *spillover effect* and can be the result of both deliberate (e.g. training of workers, quality control enforcement at suppliers or student scholarships) and non-deliberate actions (e.g. competitive pressures on local firms or the subsidiary as "benchmark", model and source of "best practices"). There are many routes and transmission mechanisms through which knowledge from the TNC parent (ultimately) can reach indigenous firms and entities. The extent of the spillover effect will depend on a very wide range of issues, including the resources and capabilities of indigenous firms, and is elusive to quantify. Nevertheless, as the foremost reason for encouraging FDI, it is the Holy Grail of FDI impact and needs to be researched carefully[4].[5]

In this context, the ASEAN region is a prime target for investigating FDI impact because it has been a major and successful recipient of investment by transnational corporations (TNCs) for three decades, albeit the scale of inward FDI flows has declined in recent years. This was the fundamental justification for the Bradford Study[6]; and one of the prospects afforded by looking at FDI in ASEAN as a whole was the opportunity to examine how the regional aspect impacted on newer member countries such as Vietnam, both in terms of direct economic benefits (especially in terms of the regional value chains of TNCs) and indirect benefits, principally – as the project was designed – with regards to the lessons that could be learned from the experience of older member countries.

The project was divided into two parts, one macro and one micro. The macro part was an econometric assessment of the *degree* to which FDI has resulted in growth and poverty reduction in ASEAN countries. The results of the macro part of the project will be discussed in the section on lessons to be drawn, but the main focus of this article will be on the micro part of the project, which examined *the detail* of the FDI impact by interviewing top Executives at TNC subsidiaries in a number of ASEAN countries. The principal issues discussed in the interviews included, the overall scale and configuration of subsidiary activity, international and regional integration, the subsidiaries role in the local economy, human resource development and future intentions in ASEAN.

A semi-structured questionnaire was used to interview managers in 5 ASEAN countries, namely Malaysia, Thailand, Singapore, Cambodia and Vietnam. There were a number of variants of the questionnaire used, especially for Singapore where most firms interviewed were regional headquarter companies (RHQs). The firms selected for interview were chosen using the following criteria:

- Industry: firms engaged in electronics/electrical and garments/textiles products (a few firms in other industries were selected as a control group and by way of comparison).
- Origins: Non-ASEAN TNCs, ASEAN TNCs and indigenous firms (the indigenous companies represented both a control group and a way of comparing competitors – and thereby competitive effects - in selected products).
- Size: appropriate levels of small to large measured by number of employees and capital.
- Locations: Penang, Kuala Lumpur and Selangor (Malaysia), Central Region, including Bangkok (Thailand), Hanoi and Ho Chi Minh City (Vietnam), Phnom Penh (Cambodia) and Singapore. These choices reflect the location of significant numbers of firms, sites of partner institutions and practical issues.

The proportions of firms selected by industry, source etc. reflected, of course, the size and rankings of TNC activity in each respect in each host country. The number of firms interviewed in each host country was based on (a) the relative size of FDI in each country; (b) the time available for the fieldwork and other resources and (c) other considerations, e.g. the fact that Singapore was in the frame mainly because it was host to most regional headquarters (RHQs) in ASEAN. The interviews were, normally, two to two and a half hours in length, though some were shorter and a few much longer. The number of interviewees varied, but in most cases the CEO, Managing Director or equivalent top executive with a sufficient oversight of the subsidiaries' overall activities participated in the interview.

A total of 113 companies were interviewed. A number of these companies were "pure" regional headquarters (RHQ) firms, i.e. they had no manufacturing activities whatsoever (although others were also engaged in manufacturing). In addition 10 companies interviewed were indigenous firms (normally direct competitors with one or more TNC subsidiaries in the sample) and some firms were in other industries (e.g. 2 automakers in Thailand) by way of comparison. Most of the quantitative information presented below relates to 88 manufacturing companies in the 5 host countries and 4 industries surveyed. Table 1 indicates the main characteristics of these 88 firms. The subsidiary companies interviewed are dispersed by source, although most are from Japan, the USA, Europe and Taiwan, in line with the overall shares of inward FDI by source in ASEAN. Most companies were established before 1996 which means that the companies interviewed have been some time in ASEAN and about a half of the parent TNCs have more than one subsidiary in the host country in which the interview took place. In other words there is a reasonable history, experience and scale to the investments. Finally, we are able to use Vietnam as a suitable case study in this paper because the relative sample size is reasonable. A full 25% of the subsidiaries interviewed are in Vietnam, whereas 31% and 28% are in Malaysia and Thailand respectively, which allows for useful comparisons, especially since Malaysia and Thailand represent the closest models in ASEAN for a country such as Vietnam to follow[7].

Table 1. Characteristics of Interviewed Companies by country of ownership, destination, period of establishment and degree of parent's involvement

Characteristic		Number, Percent	Comments
Country of Origin (number of firms and percent)	USA	12 (14%)	Concentrated in Malaysia – 7 out of 12
	Japan	27 (31%)	Fairly equally dispersed between Malaysia (10), Thailand (9) and Vietnam (7)
	Europe	11 (12%)	Biggest number in Malaysia - 5
	Taiwan	11 (12%)	Fairly equally dispersed between Malaysia (2), Thailand (4), Vietnam (3) and Cambodia (2)
	Hong Kong	8 (9%)	Fairly equally dispersed between Thailand (3), Vietnam (2) and Cambodia (2)
	Singapore	4 (4%)	Entirely in Cambodia (3) and Vietnam (1)
	South Korea	6 (7%)	Biggest number in Vietnam (3)
	Malaysia	2 (2%)	Both in Vietnam
	Other	7 (8%)	Biggest number in Thailand (4)
Host Country	Malaysia	27 (31%)	Mostly in EE (18) and CE (7)
	Thailand	25 (28%)	Mostly in EE (16) and CE (5)
	Vietnam	22 (25%)	Mostly in CE (8) and G (8)
	Cambodia	11 (12%)	Entirely in G (11)
	Singapore	3 (3%)	Entirely in EE (3)
Date Firms Started Operations (no/%)	Before 1980	14 (16%)	67% of firms in Singapore commenced operations before 1980; 33% in Malaysia
	1980-1985	8 (9%)	16% of firms in Thailand commenced operations
	1986-1990	20 (23%)	Big growth years in Malaysia (37% established in this period) and Thailand (36%)
	1991-1995	19 (22%)	Growth years in Thailand (16%), Vietnam (45%) and Cambodia (27%)
	1996-2000	19 (22%)	Growth years in Thailand (16%), Vietnam (27%) and Cambodia (54%)
	2001 or 2002	8 (9%)	Continuing expansion in Vietnam (23%) and Cambodia (18%)
Mean Ownership Share (%)		86%	Most companies (57) are wholly owned by the foreign company; only 9% are minority owned. The mean ownership by source country in reverse order is: Europe (99%), USA (94%), Japan (84%), NIEs (82%); ASEAN (77%); Other (77%)
Number of companies owned by foreign parent in host country	1	47	Nearly a half of parents have additional companies in the host country in which they are invested. This is the case for more than a half of Japanese parents (17 out of 27); Multiple companies are more common in Malaysia (17 out of 27) and Thailand (16 out of 25), reflecting longer periods of establishment.
	Over 1	41	

Source: Bradford Study.
Note: CE = Consumer Electronics; EE = Electrical and Electronics; G = Garments; T = Textiles; NIEs = Newly industrialised economies (South Korea, Taiwan and Hong Kong).

3. Direct Benefits of ASEAN Membership

Because of the focus of the Bradford Study, we will mainly confine ourselves to potential FDI related benefits accruing to a new member country, such as Vietnam. Even narrowing the focus thus, the benefits are not so easy to evaluate. Essentially, there might be four principal types of benefit: (i) a greater inflow of FDI to the country as a consequence of the "halo effect" of ASEAN membership (certainly the association was a prime target for foreign investors in the developing world while Vietnam was negotiating for membership and when it joined in 1995); (ii) a greater inflow of FDI the country's entry to the wider ASEAN market, especially in the context of AFTA (the ASEAN Free Trade Agreement) which was being put in place in the mid-1990s; (iii) a greater inflow of FDI as a consequence of the extension of regional value chains (and the consequent increase in TNC network-driven intra-ASEAN and international trade); and (iv) a greater inflow of FDI because of investment induced by ASEAN investment agreements. Inasmuch as the halo effect and market effect are more general (and hard to distinguish from each other), these will be discussed jointly; similarly, the regional value chains inherent in the latter two potential effects will also be analysed in the same subsection.

Halo and Market Effects

To put it boldly, there is little overall evidence of an ASEAN halo or market effect (table 2). Inward FDI in Vietnam began to increase sharply after 1987 when the Vietnam began to liberalise its foreign investment regime (the *Doi Moi* – "renovation" – policy), well before ASEAN entry in 1995, although it could be argued that the negotiations to join a "free market" association of countries was also a part of the liberalisation process (Gates 2000). Of course, after 1997 Vietnam suffered from the Asian economic crisis, alongside its ASEAN neighbours, but the downturn in FDI was not as severe as for some other member countries.

This implies that investors treat ASEAN countries in a differentiated way and did not lump Vietnam in with the rest – thus, even if it may not have gained from a halo effect, it also did not suffer from association with some other ASEAN countries. (More recently, Vietnam, in common with many other countries has suffered from a further collapse in inward FDI, but this largely reflects the current slump in global FDI (UNCTAD 2003)). This argument can be examined concretely by looking at the motives of investors in Vietnam (table 3) as elicited from TNC subsidiaries in the Bradford Study.

Table 2. Foreign Direct Investment Flows in Vietnam and ASEAN, 1989-2002 (US$ mn)

	1989-94 (annual average)	1995	1996	1997	1998	1999	2000	2001	2002
Brunei	4	583	654	702	573	596	600	244	1,035
Cambodia	26	162	586	-15	230	214	179	113	54
Indonesia	1,524	4,346	6,194	4,677	-356	-2,745	-4,550	-3,277	-1,523
Laos	19	88	128	86	45	52	34	24	25
Malaysia	3,964	5,816	7,296	6,324	2,714	3,895	3,788	554	3,203
Myanmar	135	277	310	387	314	253	255	123	129
Philippines	879	1,459	1,520	1,249	1,752	578	1,241	1,792	823
Singapore	4,798	8,788	8,608	10,746	6,389	11,803	5,407	8,609	7,655
Thailand	1,942	2,068	2,271	3,626	5,143	3,561	2,813	3,759	1,068
Viet Nam	651	1,780	1,803	2,587	1,700	1,484	1,289	1,300	1,200
ASEAN	13,942	25,367	29,370	30,369	18,504	19,691	11,056	13,241	13,669
Inward FDI in Vietnam, 1980-1994	Average 1980-86	1987	1988	1989	1990	1991	1992	1993	1994
	8	5	8	4	180	375	474	926	1,945

Sources: Calculated from ASEAN FDI Database and UNCTAD (2003), table B.1

The motives in table 3 were constructed from an open-ended question which asked Executives for the three most important reason why the investment had been undertaken in the host country. In the case of Vietnam all of the investments had taken place in the 1990s or early 2000s, so mostly the reasons were fresh in the memory of CEOs (and similar level Executives) interviewed. Table 3 clearly shows that ASEAN as a region or market was not a reason for investing in Vietnam as far as the 22 TNCs interviewed were concerned. The most important reasons given were: labour cost and quality (24%), Government policies and incentives (16%), size of the Vietnamese market (14%) and prior business contacts (13%).[8] Only one firm mentioned regional prospects/dynamics or regional penetration as a region. Leaving aside Cambodia as a special case (though the region is not mentioned by any interviewees in Cambodia either), it is worth mentioning that more-or-less the same profile of motives is given by investors in Malaysia and Thailand. However, regional prospects are given as 1 reason out of 5 by TNC subsidiaries in Singapore, where such motives make some sense (given the country's role as a regional hub), but since there were only 3 pure manufacturers in Singapore in the sample, not much can be deduced from this response. Since 1997 any idea that ASEAN membership might have a halo effect has, understandably, collapsed; however, the lure of ASEAN's market should not be discounted, although this will require a full implementation of AFTA (which has yet to be realised).

From the viewpoint of investors, the lack of a halo effect is not surprising. Hitherto, most manufacturing investment has been for the purpose of using local (country-level) factors for exporting to non-ASEAN, mostly developed country, markets and, in consequence, there has been little integration of the region's economies (indeed some countries have resisted AFTA and AIA because of real or perceived investment competition with ASEAN neighbours)[9]. (For further discussion and a summary of other studies, see Sakakibara and Yamakawa 2003a and 2003b.) Having said this, ASEAN has been implementing serious integration measures (such as AFTA and the AIA) since the mid-1990s and, given that so many TNCs are now based in ASEAN, opportunities now exist for them to expand or extend their activities (e.g. using local or regional reinvestment) to other South East Asian economies. If so, such activities would link in with the idea of regional value chains – to which we now turn – as a potential basis for direct benefits (our analysis below focuses on ASEAN, but see Krumm and Kharas 2003 for a discussion of developments with respect to the wider East Asian region).

Table 3. Reasons for investing in ASEAN Host Countries

Reason	Singapore		Malaysia		Thailand		Vietnam		Cambodia		Total	
	No	%	No	%	No	%	No	%	No	%	No	%
Government incentives/policies	2	40	9	13.4	12	17.9	10	16.1	2	12.5	35	16.1
Political stability	1	20	4	6.0	4	6.0	2	3.2	0	0.0	11	5.1
International trading systems	0	0	2	3.0	1	1.5	1	1.6	3	18.8	7	3.2
Economic stability	0	0	5	7.5	4	6.0	2	3.2	0	0.0	11	5.1
Growth rates	1	20	0	0.0	0	0.0	0	0.0	0	0.0	1	0.5
Size of the local market	0	0	6	9.0	3	4.5	9	14.5	0	0.0	18	8.3
Socio-cultural issues	0	0	0	0.0	3	4.5	0	0.0	0	0.0	3	1.4
Labour-related issues (cost, quality, capability development	0	0	8	11.9	15	22.4	15	24.2	3	18.8	41	18.9
Language ability	0	0	4	6.0	0	0.0	1	1.6	0	0.0	5	2.3
low production costs	0	0	3	4.5	0	0.0	1	1.6	1	6.3	5	2.3
Good infrastructure	0	0	5	7.5	0	0.0	0	0.0	0	0.0	5	2.3
Regional dynamics/prospects	1	20	1	1.5	2	3.0	1	1.6	0	0.0	5	2.3
Regional penetration (inc. intra-regional relocation)	0	0	1	1.5	0	0.0	0	0.0	0	0.0	1	0.5
Gain local market share	0	0	1	1.5	1	1.5	1	1.6	0	0.0	3	1.4
Follow customers	0	0	5	7.5	4	6.0	0	0.0	0	0.0	9	4.1
Customer recommendation/decision	0	0	1	1.5	1	1.5	1	1.6	2	12.5	5	2.3
Follow competitors	0	0	2	3.0	1	1.5	1	1.6	0	0.0	4	1.8
Brand building	0	0	1	1.5	0	0.0	0	0.0	0	0.0	1	0.5
Prior business contacts (OEM or other)	0	0	4	6.0	6	9.0	8	12.9	2	12.5	20	9.2
Rationalisation/reorganisation policy	0	0	1	1.5	4	6.0	1	1.6	0	0.0	6	2.8
Diversification policy	0	0	1	1.5	2	3.0	2	3.2	0	0.0	5	2.3
Other	0	0	3	4.5	4	6.0	6	9.7	3	18.8	16	7.4
Total	5	100	67	100.0	67	100.0	62	100.0	16	100.0	217	100.0

Source: Bradford Study.
Note: Multiple responses apply: each firm was asked to give up to three reasons for investing in the Host Country.

The Regional and Global Value Chain

With current advances in technology and the endeavour of many TNCs to focus their business on core products through global rationalisation of the value chain, Vietnam may well follow a different initial development path to that of its neighbours. Before the 1990s, Asian affiliates mainly produced mature products while parent companies concentrated on new products. Production costs were kept low thanks to low wages in developing areas.

Standardised technology was easier to use in developing countries, as few skills were required from workers. Nowadays, production has become more technology-intensive (depending on the sectors), and many affiliates in Southeast Asia receive state of the art technology. This results from TNCs' strategic decisions to select only a few manufacturing locations in the world, as part of their global value chain activities. If an affiliate is merely integrated in the TNCs' value chain as a screwdriver-type plant, it receives semi-finished parts from its parent company and assembles it. This type of affiliates used to be common a couple of decades ago in ASEAN. However, factories that manufacture parts and components in-house have increased. With more integrated plants in Southeast Asia, production of parts is either taken on by the affiliate, or performed by other affiliates in the host country or neighbouring countries. Sometimes parts are simply procured from local producers, which is when the foreign firm may have linkages with supplier firms.

In running their global operations, TNCs are faced with strategic choices over control of key functions and the balance between in-house activities and contracting to other firms. To illustrate the functional scope of affiliates across Southeast Asia, and how they are integrated with each other, we will use the example of Fujitsu, one of the companies in the Bradford study and illustrative of the hard disk drive (HDD) industry which has relocated to ASEAN to a great degree, and the global trends followed in this industry (Gourevitch et al., 2000). Fujitsu is structured around six key services and product categories[10], but also divides the world into sub-geographical units particularly for sales and marketing purposes. The company interviewed was established in 1988 in Thailand to assemble hard disk drives. Fujitsu produces 12 percent of world HDD, a half of which are assembled in Thailand. The Thai operations have no functional scope other than assembling the product. All sales and procurement functions are performed by the regional headquarters (RHQ) located in

Singapore, while overall strategy and R&D functions are performed by the parent company in Japan. Other manufacturing plants operated by Fujitsu are located throughout Southeast Asia, namely the Philippines, Malaysia, Singapore and Vietnam. Operations of the Thai plant are integrated to those of its sister companies within ASEAN. In Vietnam, Fujitsu has one representative office, one sales office and three manufacturing plants[11]. All three manufacturing/assembling plants were established after 1995, and clearly Vietnam was integrated into the regional value chain of the company later than the other ASEAN countries. This indicates how Fujitsu has penetrated ASEAN in stages, and it was only after becoming familiar with neighbouring countries and the regional environment that Fujitsu penetrated Vietnam for manufacturing purposes. The Thai operations are linked to Philippines and Vietnam for inputs and to the Singaporean RHQs for sales and marketing, while R&D is performed in Japan. The whole of the affiliate's production is sent to sales companies, and then sold world-wide (with only 10 percent sold in other ASEAN markets). About half of the affiliate's inputs originate from within the company. While a large share of these internal inputs come from Japan, many come from affiliated companies in Singapore, the Philippines and Vietnam. Thus, although the Thai plant does not manufacture for other affiliates, it uses parts and components manufactured by other Fujitsu affiliates in Singapore, the Philippines and Vietnam in its assembling activities. The assembling function of the plant is part of the global and regional value chain of the company.

Useful lessons can be learnt from the regional rationalisation and interaction of Fujitsu's affiliates in Southeast Asia. This case illustrates the extent to which business networks have been formed by multinational firms over time across Southeast Asia, including Vietnam in these networks in the 1990s. Relations between affiliates are very strong in the case of the Singapore RHQs, which overlooks activities across the region. The Vietnam manufacturing plants provide some inputs to other affiliates in the region and benefit from functional and informational support from other operations in the region. This regional orientation of firms and subsequent creation of networks in the electronics industry is documented in the literature (UNCTAD, 1993; Dobson and Chia, 1997; Borrus et al., 2000; Legewie and Meyer-Ohle, 2000; Giroud, 2004). Multinationals upgrade their technologies in certain subsidiaries, which is beneficial to other affiliates in the region, as is the case for Japanese electronics firms in East Asia (Song, 2002). The subsequent investment pattern is beneficial for host countries' development (Takatoshi and Krueger, 2000). Such networks are of a different nature in the textile and garment sector, where global strategy prevails. The location of manufacturing activities in the textile industry is volatile, focused on low-cost, skilled labour. Similarly sources of inputs may change often, depending on price and quality. In this context of global and regional organisation of activities, it is key to analyse economic indicators.

FDI and trade trends highlight the extent to which Vietnam is closely linked to its neighbour countries. Intra-ASEAN investment flows reflect the level of integration between economies in the region, whether these investments originate from locally-owned firms or foreign firms located in the region. The above analysis and case study suggest that recent years should have seen an appreciable amount of intra-ASEAN FDI and, indeed, this does seem to be the case.

Table 4 indicates that intra-ASEAN investment flows only represent 10% of the overall inward flows to member countries. This figure does not include cases when companies decide to expand further into Southeast Asia but investment comes from the parent firm as opposed to an existing affiliate in the region. The intra-regional investment flows remains limited, except for the newer member countries of ASEAN (including Cambodia for which data is not available), which are heavy recipients of FDI from neighbouring countries. However, Vietnam's experience in terms of investment attractiveness is markedly different (inflows are far higher and 20% are intra-regional inflows) from that of other new members because of its large population, political stability and diversified industrial base.

Table 4 Inward Intra-ASEAN Foreign Direct Investment Flows, 1995-2001

Host Country	Total Inflows (US$ mn)	Intra-Regional Inflows (US$ mn)	Intra-Regional Inflows as % of Total Inflows
Brunei	4,334	1,322	30.1
Cambodia	1,101	na	-
Indonesia	4,288	136	3.2
Laos	458	250	54.5
Malaysia	12,264	2,422	19.7
Myanmar	3,164	985	31.1
Philippines	10,115	1,025	10.1
Singapore	66,142	2,817	4.2
Thailand	28,545	3,903	13.6
Vietnam	11,944	2,394	20.0
Total ASEAN	142,358	15,257	10.7

Source: ASEAN Secretariat (2003), calculated from table 3.1.1

Vietnam's distinctiveness compared to the other new members of the region explains why it has received a substantial amount of inward foreign investment. Vietnam is beginning to resemble Malaysia or Thailand in terms of its attractiveness to foreign investors and during 1995-2001 it received more investment than the Philippines, a more developed country (albeit beset by political instability).[12] A fifth of inward investment in Vietnam originates from the region, the majority of which comes from Singapore (about two-thirds), Malaysia or Thailand (one-sixth each) (ASEAN Secretariat 2003). This is not unexpected given that – apart from Indonesia – these are historically the major recipients of FDI in ASEAN, they are the three most developed regional economies and host the most ASEAN TNCs and TNC RHQs (the latter are predominantly in Singapore). In addition, unlike other major recipient countries of FDI in ASEAN 70% of all inward investment in Vietnam comes from East Asia (ASEAN, Japan, South Korea, Taiwan, Hong Kong and China), with over 90% of manufacturing FDI from companies based in East Asian economies (ASEAN Secretariat 2003). Partly this is because of the dearth of inward US FDI, until recently, but this degree of regional integration (ASEAN and the rest of East Asia) also reflects the nature of the global and regional economy into which Vietnam has emerged (Krumm and Kharas 2003). East Asian TNCs are now major players on the world scene; and many non-Asian TNCs have operations across East Asia, which they can readily link into any new operations they establish in Vietnam.

Thus, from an investment perspective, Vietnam is closely linked to its neighbouring countries. This trend is also evident from a complementary trade flow analysis. In 2001, more than two thirds of Vietnam's merchandise imports originated from, and nearly half of its exports were directed to Asian countries (Asian Development Bank, 2002), which indicates the importance of the region as a whole for Vietnam's trade patterns (Sakakibara and Yamakawa 2003b). Overall, ASEAN intra-regional trade has doubled during the last decade, up from over US$ 21 billion in 1993 to over US$ 47 billion in 2001. Similarly, intra-regional imports have nearly doubled, from US$ 20 billion in 1993 to US$ 38 billion in 2001[13]. Asia as a whole is key to the economy of Vietnam representing 42% of Vietnam's total merchandise exports and 78% of the country's merchandise imports[14]. Singapore is a key partner to Vietnam, second to Japan in terms of export and first in terms of imports. Vietnam's export success is due, to a large part, to its textiles and garment industry (Hill 2000), and has mostly occurred after the *Doi Moi* reform process (Cooper 2002, Gates 2000).

In the context of foreign affiliates in the Bradford database, Vietnam's consequent current position in the ASEAN, East Asian and global value chain is shown in Table 5. The Table indicates the geographical direction of outputs in inputs produced or used by TNC subsidiaries in Vietnam and the other ASEAN countries surveyed. On the output side Vietnam seems to be strongly bifurcated between companies supplying the local market (including other manufacturers) and companies exporting beyond ASEAN. Unlike Singapore, Thailand and even Malaysia[15] little output is exported to other ASEAN countries which probably reflects the low level of component production in Vietnam, the market-orientation of some foreign firms in the country (as shown in Table 3, the size of the local market is a key motivation factor for firms investing in Vietnam, second to low-cost and skilled labour and on equal foot to government incentives) and the nature of the textile and garment industry (as half of the firms in our sample are in this industry). On the other hand, unlike other major ASEAN manufacturing bases (Malaysia and Thailand) Vietnam imports a considerable amount of inputs through intra-TNC sources from other ASEAN countries. These are then used for producing goods, which are either sold in the local market (an appreciable 40%) or sold in non-ASEAN markets. It is interesting to note that the two major sources of imports are East Asia (30% of inputs, excluding Japan) and ASEAN (23%) – but most exports go to Japan, Europe and North America. East Asia is a significant source of inputs for Thailand and Cambodia; while local/ASEAN inputs are more important for Singapore and Malaysia – Vietnam is balanced in terms of the proportion of ASEAN and East Asian inputs probably because its is being used as a major cheap, but skilled labour site for export-orientated industries by TNCs based in both ASEAN and the rest of East Asia. The size of its population and its location between ASEAN and southern China are probably also important factors.

Overall, TNCs located in Vietnam have two key final markets, the local market and predominantly developed country markets (Japan, Europe and the US). In terms of imports, however, the role of neighbouring ASEAN countries is more substantial accounting for nearly a quarter of total imports. From these data, it appears that being part of ASEAN has greatly benefited Vietnam. Recently, ASEAN economies have lost momentum in attracting new inflows of foreign investment. Interviewed companies were asked if they or their parent TNC would be investing in other ASEAN countries in the near future. Most companies (around 80 out of 88 responded), but indicated no possibility (just over 1 in a Likert scale of 1 to 5) for all countries except Thailand and Vietnam. For these the average response was just over 2 (“if the opportunity arises), which, of course, means that some TNCs were definitely considering expansion of operations to Vietnam. In this new environment, Vietnam needs to increasingly rely upon its own local advantages to continue attracting investment, and the nature of its economic relationship with neighbouring countries needs to change accordingly.

Table 5 Direction of Outputs/Exports and Direction of Inputs/Imports of Interviewed Firms

(Percentage share, reading across rows)	Local	ASEAN	Japan	East Asia	Europe	North America	Rest of the World
Total Outputs/Exports (100%)	28	7	13	8	20	22	4
Singapore	40	10	0	20	10	20	0
Malaysia	29	7	10	8	20	23	3
Thailand	26	13	14	8	14	23	2
Vietnam	40	2	21	8	10	13	10
Cambodia	0	0	1	5	57	36	0
Total Inputs/Imports (100%)	26	13	15	29	7	7	3
Singapore	2	40	5	2	10	0	40
Malaysia	35	8	22	11	13	11	0
Thailand	35	1	18	25	3	16	2
Vietnam	20	23	14	30	7	0	6
Cambodia	0	18	0	82	0	0	0

Source: Bradford Study.
Notes: Export requirements are imposed by governments on 57% of companies, but this tends to reflect their intended output orientation in any case. Local content requirements are imposed by governments on 8% of companies.

In terms of benefiting from existing investment, regional integration is expanding, with differences across industries and countries. Less than half of TNCs in the Bradford Study subdivide operations on a regional basis, and only 14 out of the 33 firms that do have such operations specifically subdivide their operations at an ASEAN level. A clear distinction appears between companies in the Electrical and Electronics industry and those in the Textile and Garment industry. Very few companies in the latter group have a regional policy, and even fewer have a policy at the ASEAN level. Of the companies that have subsidiaries in more than one ASEAN country, 35% describe the degree of integration across ASEAN operations as close or very close. In the case of companies in the textiles industry, close integration only occur when the parent company originates from another member country in ASEAN, or, in one case, integration is:

> *"…very close because most raw material comes from Malaysia. Every day, the general manager in the Vietnamese affiliate reports to his superior in Malaysia, the latter then reports the head office in Taiwan on operations across Malaysia and Vietnam. Some products are produced in Malaysian plant and then sent to Vietnam to enter into the manufacturing process."*

Clearly, this example indicates that close regional integration can take place in the case of companies in the textile and garment industry, but this is far less common than in the electronics industry. Understandably, regional integration is strongest in the case of companies which are headquartered are in ASEAN or which have a RHQs located in ASEAN. Mean score on regional integration is high in the case of affiliates located in Singapore, essentially because Singapore is attractive to higher value-added type of activities, and is hosting many of the RHQs in the region. The example of Fujitsu showed how functional areas were dispersed within the region, with R&D mostly performed in Japan, Singapore as the location for the RHQ, and other affiliates in the region essentially in charge of production and some sales and marketing. Of the 14 firms, which adopt a regional strategy and consider ASEAN as a regional entity, 12 have their RHQs located in Singapore, one in Malaysia and one in Thailand. The role and strategic orientation of each affiliate is also key to explaining the regional orientation. Slightly more than half of the TNCs in the Bradford survey are manufacturing platform and have no other strategic function. These affiliates are closely dependent on their parent firm and/or the RHQs for strategic decisions. Over two thirds of affiliates in the Textile and Garment industry have no strategic role and merely manufacture the goods, against only two fifth in the Electrical and Electronics industry. In line with the investment and development path, only 40% of affiliates in Malaysia and Thailand are mere manufacturing platform. One fifth of affiliates in these two ASEAN countries have in-house R&D facilities, and in Malaysia another fifth are completely autonomous affiliates. The picture is very different in Vietnam and Cambodia, where over three-quarters of affiliates only perform a pure manufacturing base function.

It is clear from the above that, although global factors are important in determining the overall scale of FDI and the dispersal of industries, geography does matter (a point also forcibly made by Jovanovic 2003, who reminds us of the significance of location, the international/regional division of labour and comparative advantage). The industries surveyed in the Bradford Study have located in specific countries and regions and the consequence is a series of global *and* regional value chains (the hard disk drive industry is an example par excellence of this; see McKendrick et al 2000 for a detailed analysis). Vietnam has benefited enormously from its position betwixt ASEAN and greater China and the attention of East Asian and ASEAN investors, as well as those from further afield. This explains why Asia and ASEAN account for such a large share of investment in ASEAN and the country's international trade. Affiliates in Vietnam are closely integrated in the global and regional value chains of firms, which is reflected in investment and trade flows. However, most foreign operations in Vietnam are performing pure manufacturing (or assembly) activities and these subsidiaries do not, as yet, perform higher value-added type of activities.

This is a start, especially as significant levels of FDI in emerging economies can be used to foster other developments (e.g. the utilisation of information and communication technology, see Gholami et al 2003), which leads to further investment. However, in order to avoid the danger of Vietnam becoming a loser from ASEAN regional integration (because of the potential trade divergence effects of the ASEAN regional agreement, Venables 2003[16]), the country has to diversify in terms of the range of industries TNCs establish in the country, move up the value chain and ensure that it benefits in a lasting way from FDI. In this it can learn from its partners in ASEAN who have already trod this path, an aspect to which we now turn.

4. Lessons that Vietnam can learn from other ASEAN Countries' Experience with FDI

Are there lessons that Vietnam can learn from ASEAN countries? This, effectively, was the question asked by the macro part of the Bradford Study, as mentioned in section 2. This part of the study was conducted by our colleagues Hossein Jalilian and John Weiss, both then at the University of Bradford[17]. They produced an econometric model to assess the degree to which FDI induces growth and results in poverty reduction (Jalilian and Weiss 2001). Poverty reduction was defined in terms of a fall in absolute poverty, measured using a headcount index based on the World Bank US$1 per day poverty line in purchasing power parity prices (with some allowances made for the limitations of this measure). Both developing and some developed countries were included in the model. There is insufficient space to go into the details of the macro study[18], but the gist of their results can be gleaned from the following quote:

> *"…our econometric analysis finds that FDI inflows are associated with higher economic growth, while it is in countries with higher educational levels (as proxied by* ***primary*** *school enrolment) where the FDI impact on growth is strongest. In terms of the relation between growth and poverty we find, as several others have, that there*

is a close relation between average income growth and growth of the incomes of the poor. For our larger sample of countries we find ***no*** *direct link between FDI and poverty reduction. However, turning to the question of poverty in ASEAN we find evidence that FDI in the ASEAN region is poverty-reducing and that this effect is stronger there than elsewhere (there is a poverty reducing marginal impact of 0.32, i.e. each dollar of investment has reduced poverty by 32 cents). Further there appears something special about these relationships in ASEAN, since it is only in these five countries* [those for which data was available] *that there is a direct relation between FDI and poverty reduction. On average in our sample for ASEAN roughly 40% of the poverty-reducing effect of FDI arises through economic growth and the other 60% from a direct impact*[19]*. The obvious candidates for this direct effect include labour training and direct employment of the poor. The growth effect will pick up additional job creation over time, but this mechanism is the conventional 'trickle-down' path in response to rising mean incomes. The implications of these findings are considerable. ASEAN countries are significant and special. Only in the ASEAN-5 economies (i.e. the older member countries of ASEAN*[20]*) is there an unambiguous direct link between FDI and poverty reduction…" (Mirza et al, 2003, p67-68).*

In other words, the older ASEAN member countries do have potential lessons to teach other developing countries. It is only in this developing region (before the Asia crisis, so failures must be recognised too) that there is an unambiguous and sizeable relationship between FDI inflows and poverty reduction[21] (in other countries, as much of the literature attests, the negative effects of FDI often mitigate the positive effects; in ASEAN, essentially, it has been the other way around[22]). The relative uniqueness of ASEAN countries can also be gleaned in other ways, both macro and micro. For instance, a table in UNCTAD 2002 (p150, table VI.2) which indicates the "top 20" countries to increase their export "market share" (relative to other countries) during 1985-2000 across a range of technology categories, includes 6 of the 10 ASEAN countries as "export winners" (only Brunei and the other 3 new members of ASEAN do not appear). Furthermore, Malaysia, Thailand, Singapore and Vietnam (4 of the 5 countries in the Bradford Study) are export winners across all sectors taken together – and the first 3 (the mentors in this article, if you will, of Vietnam, the 4th) are in the top 10. Given the quite wide dispersal of the other "winners", developed and developing countries, across the globe it is clear that the ASEAN cluster of countries is interesting – as are the potential lessons relating to FDI, global-regional value chains and their impact on the host economy. Moreover, there is no doubt that Vietnam has been learning. From the mid 1980s, that is well before Vietnam formally joined ASEAN or China became a major recipient of FDI, Vietnam has been an Observer in many of ASEAN's investment fora. Being a close neighbour to "miracle economies" such as Singapore, Malaysia and Thailand, it could learn about investment policies, institutional structures, export processing zones and the like. It is no accident that the three key planks of the *Doi Moi* policy were trade liberalisation, FDI promotion and recognition of private ownership (Gates 2000).

However, lest too rosy a picture be painted, the above findings (a positive link between FDI, growth and poverty reduction in ASEAN under certain conditions) are decidedly *not* an anti pro-poor growth argument (the view, essentially, that in order to reduce absolute poverty it is important to reduce income inequality). The growth and absolute poverty reduction effects in ASEAN may seem to be strong, but ASEAN is a large, diverse region, as are some of its member countries. Although the average effect across the region might be net-positive (perhaps even to a large extent), some sub-sectors, regions and locations may indeed be subject to the costs of FDI exceeding the benefits; and a nuanced approach is needed

(Kakwani 2001, Kakwani et al 2003). Furthermore, from a policy point of view, the conclusions are not clear-cut because the debate about growth/pro-poor growth is not entirely conceptually unsullied (Eastwood and Upton) and the empirical results are very mixed (Eastwood and Upton 2001, Grün and Clasen 2003, Lu and Montes 2002). For example, Peter Warr (2001) finds that the sectors in which the growth occurs apparently do not matter (based on an analysis of 6 Asian economies); and this might imply that promoting FDI in particular sectors, say, rather than others because of desired growth/pro-poor growth effects might be counterproductive. Having said this, more concretely, Vietnam has the benefit of being able to look to experiences in nearby countries[23] in terms of issues such as pro-poor growth policies. Thus, while in Malaysia and Thailand tremendous growth raised incomes for all concerned, including the poor, until the 1990s, thereby obviating concerns about inequality (which generally *increased* for both countries, with some remission in certain periods), the slowdown in growth since the Asian crisis has meant that inequalities (overall income, gender differences, ethnic discrimination etc.) – hitherto not addressed – have represented transmission lines through which the poor *have* recently suffered more than the non-poor (Bakar and Hassan 2003, Deolalikar 2002, Milanovic 2001, Kakwani et al 2003). Poverty *has* increased. All this means that Vietnam has to pay attention to pro-poor growth policies and not just those stressing growth alone.[24] This stance is relevant to the types of impact that firms have on the local economy, as will be seen below. Moreover, even general policies towards FDI/liberalisation have to be carefully designed: not all affect poverty in the same way. For instance, some analyses suggest that openness of economies to trade reduces poverty, whereas financial "openness" can have the opposite effect (Santarelli and Figini 2002, Heshmati 2003).

Table 6. Lessons for Vietnam based on a Summary of Malaysia and Thailand's Experience of FDI Effects on the Economy, Growth and Poverty Reduction

Type of FDI Effect		Degree of Impact	Evidence	Comments on Malaysian and Thai Experience	Implications for Vietnam
Direct Effects	Employment	High	The Average number of employees per interviewed subsidiary in Malaysia and Thailand is 2,699 and 3,750 respectively. Women workers represent 48% of total in Malaysia and 71% in Thailand. Average annual output is US$1,504 million in Malaysia and US$327 million in Thailand. Two thirds of subsidiaries have sister companies in both countries.	A very high level of FDI in both countries means that manufacturing TNCs employ large numbers of people. Many subsidiaries are large, resulting in a big direct impact on the economy, growth and poverty reduction. A very high proportion of workers are women and from poorer provinces.	The average number of employees in companies interviewed in Vietnam is only 86, which pales against the scale in Malaysia and Thailand (60% of subsidiaries are small, average output is US$20 million). The difference arises from age (most have been recently established); origin (ASEAN/East Asian investments can be small); and orientation (quite a few are aimed at the local market, which is small). Clearly there is a need to increase scale (although gigantism need not be the order of the day) by encouraging a wider range of industries and investors (by origin). Consideration needs to be given to issues related to location (i.e. how poorer provinces can benefit) and gender. Careful linking with ASEAN, the East Asian and global economies can maximise the net benefits of FDI.

	Training, Human Capital	High	About 90% of the workforce in Malaysian and Thai subsidiaries has been educated at secondary school level or higher. In Malaysia 1.9% of the payroll is spent on Human Resource Development; in Thailand the figure is 2.7%. Workers in both countries receive more than 6 days training each a year, often in certifiable courses. Firms rated the current level of employee skills at an average of 3.7 out of a scale of 1 to 5 (unweighted) in Malaysia and 3.4 in Thailand. The average rose to 4.0 and 3.8 respectively for pure production-related skills (i.e. excluding innovation, soft skills etc.).	Relatively advanced segments of value chains transferred to both countries, the quality of local products has to be high in order to meet expectations of international markets, many subsidiaries assigned strategic roles (e.g. related to R&D) or autonomous. High expenditures on HRD and many days devoted for training.	Vietnam has a relatively highly educated population, so 78% of the workforce in interviewed firms has been educated to at least a secondary school level. However, there is still some way to go in terms of funds spent on skills development (only 1.5% of the payroll). A policy such as the skill development fund in Malaysia (where companies are taxed 1% of payroll, but which can be recouped when workers are trained) might be useful. Vietnamese workers are currently receiving appreciably more days of training (9) than their Malaysian or Thai counterparts, but this probably reflects the recent establishment of the Vietnamese subsidiaries. Overall, firms rate Vietnamese employee skills at 3.1 (3.4 for pure production), appreciably lower than Malaysia and Thailand, but higher than might be expected given the countries' level of development. Vietnam can build strongly on these foundations.
	(Reinvestment)	Middling	Very few companies gave precise figures. The general investment was the reinvestment was occurring, but not at a rapid pace because of economic conditions.	Primary source of future FDI expansion in these economies. TNCs need to be convinced to reinvest more.	Many companies based in other parts of ASEAN indicated an interest in investing in Vietnam. This should certainly be encouraged because it will bring more jobs, a wider range of industries and link Vietnam more into the regional and global value chain. It is worth mentioning that most large and many medium TNCs from all over the world are already in ASEAN – and making profits, which can be usefully invested in Vietnam and the region.

Consumption Multipliers	Consumption	High	Not directly measured, but implied by econometric study and the fact that average company size is large and wages quite high (because of past labour shortages).	A high rise in employment and wages has led to the growth of ancillary industries. Local conglomerates have grown on the back of this expansion.	Vietnam should encourage local companies to take advantage of rising purchasing power, as in Malaysia and Thailand – ideally in manufacturing and not just retailing foreign made goods.
	Taxes	High	As above. Income taxes are collected through companies, which means that the rate of collection is high. (Corporate taxes can be low, often because of privileges granted to exporters.)	Facilitated the improvement of social benefits, infrastructural development, education and training etc. (Note careful urban planning in Malaysia as opposed to Thailand.)	Careful infrastructural development and urban planning would be wise (avoiding white elephant schemes). Considerable attention has already been given to industrial zones. Care should be taken regarding export privileges extended to foreign TNCS. Opportunities exist for a variety of social, education and other policies.
	Net Exports	High	Very high levels of exports – over 70% overseas. Although imports of inputs are also over 70%, the local value added (direct wages and salaries, local inputs) and large-scale production ensures that a high level of income stays in Malaysia and Thailand. Most foreign companies are export orientated; few are orientated towards local markets.	Local companies have not always taken advantage of the opportunity to "seize" local markets before foreigners turn their attention inwards – this now happening. Export orientation as a mainstay for economic development is unsustainable in the long run – Malaysia and Thailand need to foster domestic-orientated development.	This is not yet an issue for Vietnam and in the short run there is much to be gained from trade links with the rest of ASEAN and China/East Asia.

Value Chain Multipliers	Suppliers	Middling	In Malaysia, 73% of inputs are bought from non-affiliated companies, but only 41% of these are bought in the domestic market from *both* indigenous and foreign originated companies. A similar situation prevails in Thailand, with 68% of inputs coming from non-affiliated suppliers, with 48% of these being bought from locally based suppliers.	The import of inputs from abroad and the existence of many local foreign-owned suppliers means that there is a mid-level effect on local suppliers and hence their contribution (through wages, salaries, taxes to the multiplier effect). However, foreign-owned suppliers contribute to the value-chain multiplier too, so the main concern, in terms of the value chain multiplier, is the high level of imports.	The purchase of local inputs is lower in Vietnam than Malaysia and Thailand. Only 50% of inputs are bought from non-affiliated suppliers and, of these, about 32% are from locally based companies (indigenous and foreign). Vietnam thus has to pursue the establishment of capable local suppliers; however, the import of inputs is not yet an issue because (a) local suppliers do not exist and (b) inputs from ASEAN allow entry into regional/global value chains. A regional division of labour also implies a greater intra-industry trade.
	Distributors & Sales Orgs.	Low to Mid	Most companies in the sample are export-orientated and thus do not establish forward linkages in the domestic economy. The few that do are keen on ensuring high quality distribution, sales and service.	“Indirect exports” (i.e. sales of components/inputs to companies in Malaysia or Thailand that export their output) means that forward linkages may be even lower than they appear. (Note: the study focuses on companies manufacturing in ASEAN and so there is a sample bias – local market importers are largely excluded.)	Vietnam is currently producing quite a few consumer products in local-foreign JVs. Greater attempts should be made to learn sales and marketing skills, rather than simply benefit from a share in high profit rates. A large population, with rising incomes gives Vietnam some leverage in this respect.

	International links	High	The companies interviewed export over 70% of output in both Malaysia and Thailand, while about two-thirds of inputs are imported. While exports and imports from/to Japan and North America are high for subsidiaries in both countries (US firms and trade figure more highly in Malaysia, Japanese in Thailand), European firms (hence trade) are far more important for Malaysia and East Asian imports for Thailand. ASEAN trade is small: firms in Malaysia import 8% of inputs from ASEAN, while firms in Thailand export 11% of outputs to ASEAN.	This results in sizeable exports by value, but high international linkages are a source of concern when too large a share is imported. One key issue is to improve the local supplier base. There are considerable opportunities for regional value chains, especially taken up by ASEAN TNCs and Consumer Electronics firms (among others).	Still low linkages in terms of overall scale, but in directionality Vietnam is similar to Thailand – though US links are largely absent and there is a large level of input import from ASEAN (23% of imports by interviewed companies). This represents an incipient regional value chain (especially with Singapore, Malaysia and Thailand), which can be developed. East Asia's share of input imports is 30%, which implies that the country could look to a wider East Asian regional grouping than ASEAN (perhaps ASEAN+3 makes more sense for Vietnam and other ASEAN countries).

Spillover Effects (training, competitive effects, demonstration effects and Human mobility)	Suppliers	Middling	Of those firms which buy inputs from local suppliers, only 7% buy high-technology goods from these companies, otherwise purchases are low tech (42%) or secondary inputs (51%). Nevertheless, local suppliers are provided with knowledge and support in terms of the goods the produce. Among interviewed firms in Malaysia, the likelihood of product specification transfer is very high at 4.64 (on a scale of 1 to 5) and the figure is similar in Thailand at 4.41. Transfer of other types of knowledge or support is somewhat lower (mostly between 2-3 depending on type for Malaysia and around 2 for Thailand). Foreign firms are somewhat more supportive of suppliers in Malaysia (52% have a supplier partnership scheme) than Thailand (32%). Overall there has been considerable improvement in the direct production-related skills of local suppliers (cost, quality, delivery), the degree of improvement being rated at an average of 3.6 (on a scale of 1 to 4) for Malaysian suppliers and 3.1 for Thai suppliers. Improvements in other types of skills (innovation, design, commercial skills etc.) were deemed somewhat lower, though the overall level was higher for local suppliers in Malaysia.	There is little room for spillovers in high-technology areas, but international supply chains mean that "world standard" technology, knowledge and expertise is imparted or seeps to suppliers. At present this largely relates to skills necessary for direct production (cost, quality, delivery, inventory control, lead-time performance), but these are a basis for moving up the value chain. There is a considerable need to support local suppliers, especially to allow them to compete in higher technology or value inputs, often against foreign suppliers based locally. Although some R&D is done locally, there is little opportunity for skills related to innovation, design etc. to seep to local suppliers and other firms. Policies to encourage this are necessary.	Vietnamese companies have to get to the first few rungs of (a) having sufficient foreign plants to supply and (b) developing a wider supplier base. At present, to the extent it occurs, transfer of product specifications to local firms is only 3.1 (on a scale of 1 to 5) and between 1 and 2 in terms of other types of knowledge. There are no supplier partnership schemes (among the firms interviewed) – but then there is the need for a critical mass of suppliers for such activities to occur – and the firms interviewed rank the improvement in local suppliers at only 2.4 compared to 3.6 in Malaysia (but bear in mind that these are much younger relationships). Vietnam clearly has to give priority to its supplier base, the quality of suppliers and the relationships between suppliers and foreign subsidiaries.
	Distributors & Sales Orgs.	Low	As mentioned above, there are few forward links with local distributors etc. because of the export orientation of foreign firms.	As earlier. Sales subsidiaries importing consumption goods might be significant in spillover effects (but these are not part of this study).	As earlier.

	Competitors	Low to Mid	Very few companies interviewed had significant direct competition from local companies, although there were some examples in garments, consumer electronics and electronic components. These included, air conditioners, white and brown goods and semiconductors.	A long way to go, but this study has identified a number of mechanisms and routes being taken by exemplar local firms attempting to become significant players in their own right in Malaysia and Thailand. These included locally-owned conglomerates which have entered new industries because foreign firms have established a market (demonstration effect, e.g. air-conditioners and consumer electronics), created local engineering and managerial expertise ("spin-off" or "silicon valley effects", e.g. semiconductor components manufacturers) or worked with foreign partners (joint ventures and similar, i.e. "learning by doing together")	As with suppliers, Vietnam has to encourage the development of local companies that can take advantage of mechanisms such as the demonstration effect, spin-offs and learning by doing. In this study there was one Vietnamese company making progress in improving its core products, technology and expertise through effective joint ventures with a number of foreign partners. Many more such companies are needed.
	Human Capital	Low to Mid	Considerable human capital of a high calibre has been generated by foreign companies in Malaysia and Thailand (see under "direct effects") above, but only a minimal level finds its way to locally owned suppliers, other manufacturers, spin-offs etc.	Policies to improve the use of skilled labour by local companies are essential. This might require some re-orientation away from export-orientated development, towards local markets and needs. Foreign companies should be encouraged to create and impart scientific, engineering and design skills as well as production skills. There is also the issue of the "loss" of skilled women workers back to provinces and other occupations.	As earlier under training.

Source: Bradford Study. **Note:** The data in the "evidence" column is drawn from 27 Malaysian, 25 Thai and 22 Vietnamese subsidiary companies in the sample.

In a similar vein to the above discussion, the macro part of the Bradford Study clearly implies "limits" to the ASEAN model, i.e. it is incumbent on Vietnam's policy makers to learn lessons about what to avoid when it comes to TNCs and FDI. The econometric analysis shows that 60% of the poverty reduction occurring in the ASEAN countries examined was through direct effects (such as employment, training) and the rest through indirect growth effects. In other words, *development and poverty reduction in most ASEAN economies is largely a scale effect and the Holy Grail of spillover effects has been scarcely glimpsed*. This can be expressed diagrammatically in figure 1, which depicts, in stylised form, the relative contribution of the three types of FDI impact (as discussed in section 2) over a period of time. If the macro results of the Bradford study are correct, then ASEAN economies are still on the left side of the diagram – and have gained little from the value chain multiplier (though the consumption multiplier effects might be appreciable because these are largely proportional to the direct effect) and spillover effect. Vietnam and other developing countries need to learn from this, but where should they put their efforts?

Some of the answers lie in the results of the micro part of the Bradford Study. It is not possible to look at the micro study in detail here (see Mirza et al 2003[25]), but the rest of this section concentrates at lessons for Vietnam arising out of the micro study, using Malaysia and Thailand as exemplars.

Figure 1. Stylised Impact of FDI: The Changing Relative Contribution of Direct, Multiplier and Spillover Effects over Time

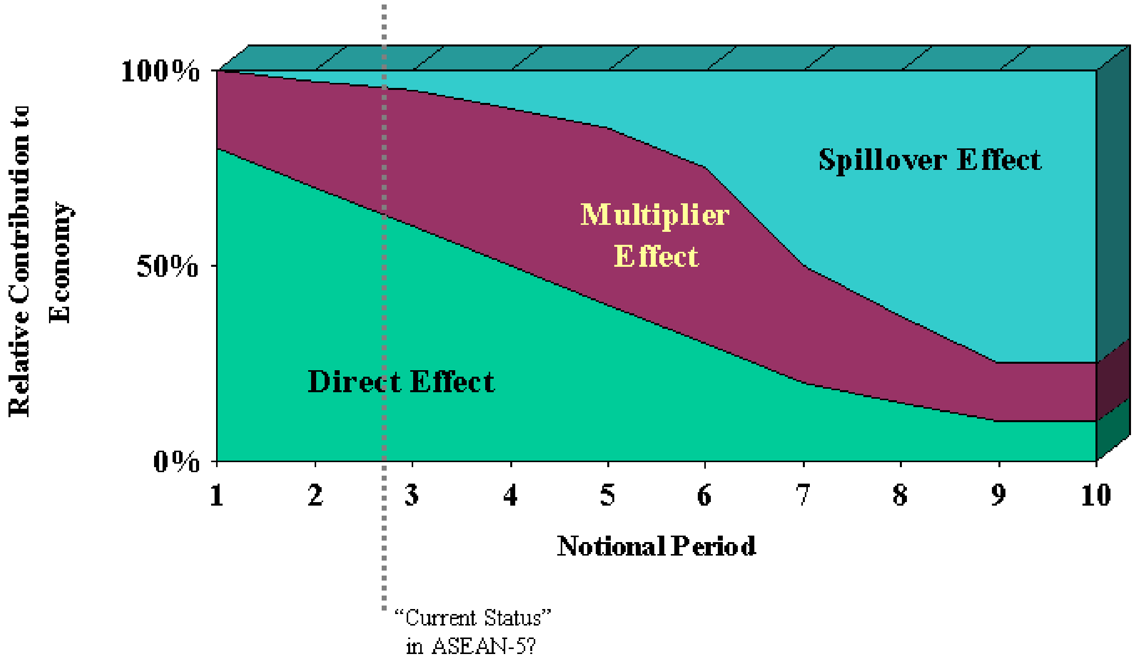

Table 6 summarises the main results of the micro-study (the bulk of firms interviewed were from Malaysia, Thailand and Vietnam) in terms of the key types of FDI impact: direct effects, consumption multipliers, value chain multipliers and spillover effects. In general, the findings (chiefly relating to Malaysia and Thailand because these were key ASEAN countries in the macro-study) are in accord with the Jalilian and Weiss' econometric results. The direct effects are very high for Malaysia and Thailand (but not yet Vietnam), although more can be done to encourage reinvestment locally and in the region. This is primarily because of the sheer scale of investment and investors: the average size of subsidiaries interviewed in Malaysia and Thailand is in the region of 2,700 and 3,750 employees respectively. In consequence, relatively high wages in these countries means that there is a high consumption multiplier, including income and expenditure taxes (probably not corporate taxes) which have been used by the respective governments for infrastructural development, social benefits etc. Malaysia is the better exemplar in terms of government use of tax yields. On the other hand, the value chain multiplier is middling, because the export-orientation of most manufacturers has meant few forward linkages in Malaysia and Thailand; and a lack of local suppliers or other concerns (for example about supplier capabilities or quality) has led to a high level of input imports and, therefore, a truncated development of backward linkages. The arrival of foreign-owned suppliers has improved the situation in terms of the value-chain multiplier (their employees also engage in consumption etc.), but in some ways this militates against spillovers to local concerns. Finally, apart from skills and activities (in suppliers and some indigenous competitor companies) related to direct production, the spillover effects of knowledge and capabilities in Malaysia and Thailand are low, despite high potential (e.g. because of the development of quite high levels of human capital). Largely this is because Malaysian and Thai companies with resources have hitherto directed their efforts into non-manufacturing areas and their respective governments did not emphasise or effectively encourage the development of significant, capable indigenous companies and champions. It is essential to do this if the Malaysian and Thai economies (and Vietnam's) are to benefit from spillovers in the future.

Table 6 also provides lessons arising from the above analysis for Vietnam. The table provides evidence (from the Bradford Study) to substantiate the findings on direct impact, comments on these and discusses the implications for Vietnam in a very detailed away. In summary, some crucial lessons are as follows. Inasmuch as Vietnam can follow the Malaysian and Thai development path, which has relied heavily on TNCs, the country should encourage further FDI in order to benefit from the type of scale effects enjoyed by these two economies. Of course, care needs to be taken regarding industries established, countries of origin (diversification, certainly, on both counts), location of investment and other issues, such as gender effects. It is also essential to support a development of local supplier, competitor and champion companies, but in parallel with foreign investors (these have the advanced knowledge from which, for example, supplying companies can learn. It is also worth encouraging Vietnam's involvement in regional value chains (in ASEAN and East Asia) because much of the new investment in the country will most likely be funded by TNCs already established in nearby countries (as well as ASEAN and East Asian TNCs). Vietnam's highly educated workforce gives it a key advantage compared to other developing countries, but much needs to be done to ensure the transfer of knowledge and skills to the workforce – as well as to indigenous suppliers and other companies. Furthermore, if Vietnam (in due course) is to reap the benefits of spillovers then local firms have to develop absorptive capacities (for knowledge/skills): of course, these will most likely be developed in tandem with foreign investors in an iterative manner. Finally, table 6 also suggests some lessons in the form of specific policies applied by Malaysia and Thailand (e.g. the skills development fund), although these need careful articulation.

5. Concluding Remarks

This article has investigated whether, and to what degree, Vietnam (as a case in point, a new member country of ASEAN and a good example of a developing country) has benefited from foreign direct investment (FDI), and its various impacts, since the country's entry into ASEAN in 1995. The investigation has consisted of a number of parts, including an assessment of "halo" and market creation effects, linkages into the regional and global value chain and the extent to which Vietnam has benefited from lessons learned from the experience of other ASEAN countries. The halo and market effects were examined together and the short discussion showed that there was little evidence of either affecting the entry of TNCs into Vietnam. The lack of a halo effect is perhaps not surprising given the advent of the

Asian Financial and Economic Crisis in 1997, 2 years subsequent to Vietnam's entry – indeed, the obverse (a contagion effect) may have applied. Nevertheless, the extent to which FDI flows held up in Vietnam (and a number of other ASEAN economies) is a testament to the fundamental robustness of the economy, as perceived by TNCs. The market creation effect (i.e. the notion that TNCs enter Vietnam because of access to the wider ASEAN market, especially because of implementation of the ASEAN Free Trade Agreement, AFTA) is also not evident from the data. Hitherto, foreign companies (at least those in the Bradford Study) have entered Vietnam and other ASEAN countries for a wide variety of reasons, but the wider ASEAN market does not figure highly in their calculations. This is not surprising, following our investigation of the nature of recent subsidiary companies established in the country. The vast majority of these are linked into global and regional value chains (and for Vietnam there are two relevant "regions", ASEAN and the rest of East Asia). In the context of ASEAN, inasmuch as subsidiaries based in Vietnam are linked to the regional value chain, their primary roles are either as suppliers of final products to the global market (using inputs from sister plants in ASEAN) or, more likely, as branch plants to principal sister plants in other ASEAN countries. In other words, the Vietnamese based factories supply inputs to more advanced factories in, say Thailand or Malaysia; and the product of the latter plants is then shipped regionally or globally. In any case, the wider ASEAN market is not the issue here, but rather existing or incipient regional-global value chains. This section of the article concludes that TNC subsidiaries in Vietnam are closely integrated into regional-global value chains, that ASEAN-based TNCs (both local and non-ASEAN) are a very promising source for further investment of this sort into Vietnam (for example, through reinvestment of profits made in nearby countries), but Vietnam has to be careful to ensure that affiliates located within its borders steadily move up the value chain – and, also, other policies are followed to maximise the benefits of involvement in regional value chains (e.g. by diversifying the industries entering, education policies etc.).

The above discussion led nicely into the final part of the article, which discussed the lessons that Vietnam could learn from other ASEAN countries, especially two exemplar countries, Malaysia and Thailand. Using the results of an econometric study of FDI flows into ASEAN and other countries (this study was conducted as part of the Bradford research by two colleagues), we initially established that the impact of FDI on growth and development in ASEAN (specifically absolute poverty reduction) is considerable and unambiguous (compared to other developing countries) and therefore Vietnam can learn from nearby countries. However, the lessons to be learned should consist of understanding failures, as well as successes, especially because, according to the econometric study, *development and poverty reduction in most ASEAN economies is largely a scale effect and the Holy Grail of spillover effects has scarcely been glimpsed.* The reasons why this is the case is explained by a careful scrutiny of the impact of TNC subsidiaries in table 6, and the accompanying text, in terms of 4 principal types of potential effect – direct effects, consumption multipliers, value chain multipliers and spillovers – and a number of sub-effects. The direct effects of FDI (essentially employment, training and skill development) have been very high in Malaysia and Thailand, mostly because of the scale of FDI, the large size of subsidiaries and the relative advanced technologies employed. Vietnam still has a long way to go in terms of replicating this experience and can certainly learn lessons relating to policy and tactics. The consumption multipliers (consumption, taxes) are also high in Malaysia and Thailand – mostly because they are largely proportional to the direct effect – and among the key lessons for Vietnam here is the need to channel these multipliers towards socially desirable goals and infrastructural investment. On the other hand, both Malaysia and Thailand have experienced relatively low levels of value-chain multipliers and spillover effects. Partly this is because of the nature of the foreign investment (e.g. export-orientated manufacturing subsidiaries means that there is little development of forward linkages; or quality assurance priority issues require that high-tech products are bought from foreign companies, either from abroad or from subsidiaries in the host country), but some of the blame can be laid at the feet of ASEAN government and company policies and strategies which have not encouraged the establishment of sufficient numbers of local manufacturing firms able to link effectively with foreign subsidiaries. The irony is that much of the necessary human, financial and other resources exist or have been created by TNCs through the direct effects mentioned earlier. Vietnam certainly can learn lessons from such failures, not least in developing absorptive capacities in local enterprises. Having said this, successful examples of spillovers do exist and were uncovered – to an extent – in the Bradford Study, thereby demonstrating how spillovers can be deepened and extended in all ASEAN economies, including Vietnam and other new member countries.

This article only represents a start in examining the complex issues relating to the lessons that Vietnam and other countries can learn from the experience of older ASEAN member countries in FDI absorption and management. Our aim is to further deepen the analysis by exploring the existing data set in depth (e.g. using more advanced analytical techniques) and, later, by extending the analysis to take in responses from other actors, including local suppliers, competitors and workers.

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NOTES

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[1] However, although the project on which this article is based looks at FDI and its association with poverty reduction, this issue will not be tackled directly except, briefly, at the start of section 4. This article is concerned solely with the benefits and lessons new member countries can derive from their association with ASEAN.
[2] The "AFTA effect" has also eased the trend towards greater investment cooperation. AFTA (the ASEAN Free Trade Area) means that a member country with a restrictive investment regime can still be serviced through trade routes by a TNC producing in another country and exporting to the former. Under such conditions, the economic argument for protecting or restricting investment flows to a certain industry or country becomes weak. If an industry or a country's market can be serviced through trade route then there is little point in restricting FDI flow and this realisation has made ASEAN countries more receptive towards investment cooperation
[3] This research study was funded by the UK Department for International Development (DfID) and was part of the Globalisation and Poverty Research Programme, under the direction of John Humphrey at the Institute of Development Studies (IDS), University of Sussex.
[4] In theory, if there were no spillovers then a TNCs departure would simply reverse the direct and multiplier effects.
[5] For fuller details of the model see the project's main report, Mirza et al (2003) at www.gapresearch.org.
[6] Again see Mirza et al (2003) at www.gapresearch.org.
[7] See Mirza et al, ibid, for further comparisons of ASEAN economies. However, in short, Malaysia and Thailand are the best regional models for Vietnam for a number of reasons: (a) they fundamentally resemble Vietnam in many respects, especially Thailand, in terms of development and economic characteristics (e.g. substantial pool of trained and untrained labour) and are not "too" far ahead in terms of GDP per Capita or other unique characteristics (unlike Singapore and Brunei); (b) the possess substantial FDI in a range of industries (unlike Cambodia, Laos and Myanmar); and (c) are relatively successful in attracting, retaining and benefiting from FDI (unlike, certainly recently, Indonesia and the Philippines).
[8] Of course, non-ASEAN and ASEAN TNCs utilising the regional division of labour might give some of these reasons, but these relates more to the regional value chain than the halo/market effect.
[9] Of course, the reality is not so extreme and companies such as Seagate have long maintained integrated chains of activity with their own subsidiaries and associated companies across ASEAN (McKendrick et al 2000); Madani (2001) also describes more long term intra-regional trade in South East Asia.
[10] These categories include (1) IT & Computers, (2) Peripherals, (3) Telecommunications, (4) Microelectronics, (5) Software, (6) Speciality Products. http://www.fujitsu.com/products/
[11] http://vn.fujitsu.com/sitemap
[12] And, of course, far more inward FDI than Indonesia which has been losing investment because of considerable turmoil.
[13] http://www.aseansec.org/trade/files
[14] http://www.adb.org/Documents/Books/Key_Indicators/2003/
[15] Cambodia is a special case: virtually all FDI is in garment production and orientated towards developed economies that have offered tariff-free import quotas to garment exports from the country.
[16] Essentially the argument is that in south-south arrangements there is the danger that the relatively advanced members specialise in more sophisticated manufacturing and service products, leaving the lower value added industries to less advanced members – hence a divergence, especially in income per capita. However, because of the existing divergence of incomes between ASEAN member countries, the association might be regarded as more akin to a "north-south agreement" (which has better prospects); and in any case, the results, are potentially more positive in the context of competitive global-regional value chains.
[17] Weiss is now at the Asian Development Bank Institute in Tokyo.
18 The paper by Hossein and Jalilian can also be found at www.gapresearch.org.
19 These percentages are based on implied marginal direct, growth and total effects of FDI reported in table (9). These in turn are based on derivation of growth of income of the poor with respect to FDI. Formally this derivation can be stated as:

$$dg^p / dfd = \partial g^p / \partial g * \partial g / \partial fd + \partial g^p / \partial fd$$

where fd stands for FDI. Based on equations (1) and (3), the first term on the right hand side is equal to $\beta_3 \mu_1$ and the second term to μ_3. From the first term we can calculate the indirect, 'trickle-down' effect of FDI and from the second term its direct effect.

[20] Indonesia, Malaysia, the Philippines, Singapore and Thailand.
[21] With growth as a principal intervening variable. See Chowdhury and Mavrotas (2003) who use an innovative methodology that shows a bi-directional causality between FDI and growth in Malaysia and Thailand (as opposed to Chile where the causality is one way, from growth to FDI).
[22] Which is not to argue that the net effect is always positive – as discussed later in this section.
[23] As well as its own experiences over the last few years, as discussed in some of the other articles in this issue of JAPE.
[24] This discussion is part of a broader debate on globalisation, development and growth, which will not be entered into here (Pyatt 2001, Asra and Santos-Francisco 2001, Mayer-Foulkes 2002, Murshed 2003, Dowrick and Akmal 2003, Laderchi et al 2003, Kanbur 2003, Franco 2003).
[25]For fuller details see the project's main report, Mirza et al (2003) at www.gapresearch.org.