TOWARDS A RETURN OF INDUSTRIAL POLICY?
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FDI, Financial Constraints, and Productivity: Firm Level Study in Vietnam

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Introduction

- Foreign direct investment is the key engine of productivity growth for developing countries.

- Recent studies also highlight the importance of financial markets in inducing innovation and entrepreneurship (Alfaro et al., 2004).

- The present paper examines the contributions of foreign investment and financial constraints to productivity growth, using a panel of 5,302 firms in Vietnam spanning over the period 2002-2008.

Why Firms in Vietnam?

- Foreign ownership has been increasingly important to output and employment growth in the Vietnamese economy.

- The past decade witnessed rapid proliferation of multinational activities as a result of its market-driven momentum toward trade and investment liberalization, coupled with policy initiatives (tax exemption, legal reform, and improved institutional infrastructure).

Table 2. Output and Employment Growth by Ownership, 2000–2008

	Output Growth (% p.a.)	Employment Growth (% p.a.)
Total	7.5	2.3
State	6.8	1.85
Non-state	7.3	1.93
Foreign Firms	10.4	20.41

Source: General Statistics Office, Vietnam.

Table 3. Surveyed Firms by Foreign Ownership Characteristics

	2002	2003	2004	2005	2006	2007	2008
	Number of Firms						
Total	**51680**	**62908**	**72012**	**91756**	**112950**	**131318**	**155771**
Foreign Firms	**2011**	**2308**	**2641**	**3156**	**3697**	**4220**	**4961**
100% foreign capital	1294	1561	1869	2335	2852	3342	4018
Joint venture	717	747	772	821	845	878	943
	Percentage of Firms						
Total	**100.00**	**100.00**	**100.00**	**100.00**	**100.00**	**100.00**	**100.00**
Foreign Firms	**3.89**	**3.67**	**3.67**	**3.44**	**3.27**	**3.21**	**3.19**
100% foreign capital	2.50	2.48	2.60	2.55	2.52	2.54	2.58
Joint venture	1.39	1.19	1.07	0.89	0.75	0.67	0.61

Source: General Statistics Office, Vietnam.

Existing Studies

- Evidence from developing countries highlights that foreign affiliates exhibit higher productivity performance than do domestic-owned firms.

- Aitken and Harrison (1999) for Venezuela; Arnold and Javorcik (2009) for Indonesia; Sabirianova et al. (2005) for the Czech Republic; and Javorcik (2004) for Lithuania.

- However, these studies focus on a productivity comparison between domestic and foreign-owned firms.

Existing Studies

- Much research points to the negative effects of financial constraints on firm survival and development (Levine, 2005; Beck et al., 2005; and Demirguc-Kunt and Maksimovic, 1998).

- Alfaro et al. (2006) show that firms in countries with well-developed financial market tend to experience positive gains from FDI.

- This issue is vital especially in developing countries where financial market development is usually limited.

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s of human capital utilization (e.g. R&D,
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