Climateworks CENTRE

BRIEFING PAPER 4

ENABLING INVESTMENT FOR VIETNAM'S ENERGY TRANSITION

LANDSCAPE OF SUSTAINABLE FINANCE

This paper is part of the Australia-Vietnam Green Economy Program, an initiative by Asialink and Climateworks Centre

The Australia-Vietnam Green Economy Program, with its capstone summit, will drive new collaboration between Australian and Vietnamese businesses in the green economy, create trade and investment opportunities, and build connections among leading experts in the bilateral relationship. Pre-summit papers and training programs will enhance Australian businesses' knowledge, capacity and connections to seize opportunities in Vietnam's green economy.

Find out more about the program

Asialink

Asialink is Australia's national centre for Asia capability and engagement working to create a better future with Asia.

Through our sustained engagement, impactful partnerships and signature offerings, we empower individuals, organisations, and governments with knowledge and capability to engage effectively in the region.

We have deep expertise across arts, business, education and diplomacy working towards one goal: to create a better future, one where Asia and Australia thrive together in our region.

Climateworks Centre

Climateworks Centre bridges the gap between research and climate action. We are climate transition specialists, working in Australia, Southeast Asia and the Pacific with decision-makers who have the power to reduce emissions at scale. Climateworks develops evidence-based solutions to accelerate emissions reduction in line with the global 1.5°C temperature goal and shared climate safety.

Co-founded by philanthropy and Monash University, Climateworks is an independent not-for-profit working within the Monash Sustainable Development Institute.

What do we mean by "Green Economy"?

Asialink and Climateworks Centre define the concept of the "green economy" in this briefing series as:

"An economic policy framework that supports national energy needs based on renewable resources, net-zero greenhouse gas emissions, and maximum contribution to human well-being and social equity."

This framework must be designed to curb emissions, reduce environmental risks, safeguard ecosystems, increase resilience of energy systems through effective governance, harness low-carbon technologies and promote sustainable practices. As such, the policy briefing series developed within the Australian-Vietnam Green Economy Program will focus on areas that could create strong synergies and leverage economic competitive advantages between Australia and Vietnam, such as the regulatory challenge of the energy transition (including the needs of end-users), access to sustainable finance, skills formation, and technological innovation.

Executive Summary

Vietnam's rise to middle-income country status has been almost singular in its pace, typified by threefold growth in per-capita GDP over the past twenty years and an 11 per cent decline in the poverty rate in the last decade alone. The sources of this growth, while multifaceted, have been driven by the Đổi Mới reforms that have taken Vietnam from centrally planned to increasingly market-oriented, comprising the establishment of closely managed financial and capital market mechanisms, targeted privatisation and liberalisation measures, and the concurrent expansion of free trade agreements and trade partnerships, 16 of which are now active (VCCI WTO Centre 2023). Vietnam's highly trade-oriented development – exports have grown to 93.3 percent of GDP – has been increasingly driven by energy-intensive manufactured goods and industrial products, leading to rapid emissions growth (Minh et al. 2023).

Accelerated economic growth and inwards foreign investment spurred demand for energy especially in carbon intensive sectors. Energy demand in Vietnam is projected to increase fourfold by 2050. Industrial sectors, including mining, manufacturing, construction, electricity, water and gas, represent just over 33 per cent of GDP, with manufacturing comprising half of that share (OECD 2021; World Bank & the Institute of Finance & Sustainability [WB & IFS] 2022).

In turn, growth in productive capacity has been tightly correlated with inward capital flows, as attendant foreign investment reforms have anchored a strong enabling environment conducive to international investment (Choi et al. 2021). A positive correlation between foreign investment and CO_2 emissions in Vietnam has also been found (Minh et al. 2023).

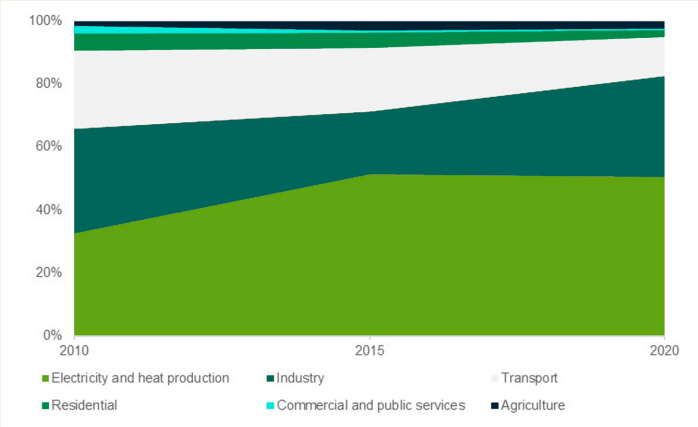


Figure 1. CO_2 emissions by sector in Vietnam: 2010-2020
Source: IEA (2023)

Between Vietnam's rapidly rising emissions, future energy demand, and signals of growing climate ambition, there is significant opportunity and a need to adapt Vietnam's robust investment environment to incentivise higher flows of capital into low-carbon activities. On the one hand, increasing climate ambitions helps to create momentum for international public finance through international development and overseas development assistance programmes to support Vietnam to achieve their development goals. The announcement of the Just Energy Transition Partnership, together with increasing climate financing from bilateral and multilateral donors, will provide opportunities to catalyse private financing to support the energy transition. On the other hand, Vietnam wants to attract more private foreign investment to green sectors, primarily through foreign portfolio investment or through foreign indirect investment. Targets set through the country's Nationally Determined Contribution, Green Growth Strategy, Power Development Plan, and the Just Energy Transition Partnership, can provide more incentives to attract investment through push policies.

This policy brief addresses the landscape of sustainable finance policy and market development in Vietnam, focusing on the country's clean energy transition. This is due to its significant emissions share and decarbonisation potential, and its central role in the government's emissions reduction agenda.

Section 1 of this brief summarises the current state of low-carbon investment in Vietnam's transition, with a focus on clean energy flows, including types of investment, investment gaps and the roles of public and private finance.

Section 2 presents a framework encompassing key elements of Vietnam's enabling environment for low-carbon investment. It addresses the strengths, challenges and opportunities for coordinated partnership between the Vietnamese government and Australian public and private sectors, in relation to the country's energy transition.

Section 3 provides a summary of the opportunities for coordinated action by the Australian government and private sector in Vietnam's transition.

1. Current state of low-carbon investment in Vietnam

The decoupling of economic growth and energy intensity is a central enabler for Vietnam to realise its development and climate objectives concurrently.

The impetus for accelerated decarbonisation is framed by dual long-term objectives set by the Vietnamese government: to reach net zero by 2050, and to become a high-income country by 2045. In order to achieve these concurrently, a wholesale shift to decouple economic and emissions growth will be required, needing a progressive reorientation of investment flows into low-carbon activities.

The scale of capital required to accelerate Vietnam's path to decarbonisation, particularly in the energy sector, needs a range of financing sources, instruments and approaches spanning domestic and international flows. Broadly, these can be split between private and public flows, although philanthropic grants can also play an important role in improving project feasibility, and providing technical assistance and capacity building in local contexts.

1.1. Typologies of foreign investment

1.1.1. Private foreign investment sources

Vietnam's strong enabling environment and export orientation present significant opportunities for the use of foreign direct investment by energy and non-energy investors, to scale clean energy uptake.

Key categories of international private finance relevant to Vietnam's transition include foreign direct investment (FDI), foreign portfolio investment, and commercial loans. FDI currently constitutes the most important source of foreign investment in the country's energy transition due to Vietnam's strong institutional framework and related incentives (see Section 2.1.1). Vietnam was the second largest FDI destination for renewable energy investment among developing economies between 2015 and 2022 (UNCTAD, 2023).

Type	Summary	Relevance
Foreign direct investment (FDI)	• Long-term, active establishment and ownership of assets by international investors. • Key types of FDI include greenfield projects, project finance, and cross-border mergers and acquisitions (M&A). • FDI is the major type of investment for Vietnam's low-carbon transition due to long-term time horizons required for the establishment of clean energy and industry, and low-carbon manufacturing development	High
Commercial loans	• In the context of Vietnam's transition, a commercial loan is a bilateral or syndicated loan provided to a Vietnamese company by a foreign commercial institution. • New regulations on cross-border lending issued through Circular 8/2023 by the State Bank of Vietnam in July have removed a number of constraints posed by Circular 12/2014, creating more favourable conditions for cross-border commercial loans that can be made for onward low-carbon sector lending (see Allens 2023a,b).	Medium - high
Foreign portfolio investment	• Indirect, 'passive' international investments in financial securities, including bonds, shares and other instruments. • Can play a more significant role in Vietnam's low-carbon transition, but Vietnam's stock and capital markets remain nascent - yet to reach emerging market status. Key barriers include foreign ownership, information asymmetry and liquidity risks (Pham et al. 2023).	Medium

While FDI and commercial loans play a relatively larger role in industrialised economies with more highly established capital and securities markets, FDI is particularly instrumental to emerging market transitions. Vietnam's high export orientation provides a strong basis for clean energy FDI particularly as, globally, an increasingly large portion of greenfield investments and cross-border M&A into clean energy projects originates from outside the energy sector, with companies increasingly investing in commercial and industrial (C&I) renewables capacity (OECD 2022).

International clean energy investment in this sense is not limited to a decarbonisation imperative for Vietnam: It is also a corporate imperative.

Particularly in Vietnam's sizeable manufacturing sector, the availability of clean energy is central to large companies meeting their emissions reduction targets. IEEFA (2022), for example, estimates that global corporations responsible for approximately US$150 billion of Vietnam's export revenues have made specific carbon neutrality commitments, with a number of companies targeting 100 per cent clean energy targets within this decade.

Additionally, the introduction of the EU's Carbon Border Adjustment Mechanism (CBAM), the impact of which will grow as covered sectors continue to expand (Chu et al. 2023), will have implications for industrial exporters, and serves as another push factor driving facility-level clean energy uptake.

FDI in Clean Manufacturing

- The Case of LEGO Group

The decision by the LEGO group to build its first ever carbon neutral factory in the southern Binh Duong Province underscores the sizable potential for FDI to assist the uptake of clean energy that supports low-carbon manufacturing in Vietnam.

The factory, a US$1 billion greenfield investment, will be co-developed with the Vietnam Singapore Industrial Park Joint Venture Company (VSIP), a partnership between Sembcorp (under Temasek Holdings) and Becamex IDC Corporation, a Vietnamese state owned enterprise.

Once operational, LEGO's Vietnamese manufacturing site will be a central enabler for the company to reach its 2032 emissions reduction target of 27 per cent below 2019 levels. The General Manager of LEGO Group explained that a strong guiding influence in selecting Vietnam was the country's 2050 net zero target.

LEGO's facility will deploy rooftop solar, and a larger-scale commercial and industrial solar project will be developed by VSIP, providing a blueprint for how coordinated action between FDI providers and government can accelerate clean energy uptake in Vietnam. This investment also exemplifies how a green supply chain could provide a comparative advantage for Vietnam to attract foreign investment.

Sources: LEGO Group 2021; The Investor 2023

1.1.2. Public investment sources

International public finance constitutes an important catalyst for scaling private sector investment in Vietnam's transition.

Public financing from bilateral partners and Development Financial Institutions (DFIs) can play a crucial role in incentivising private investment through the strategic deployment of below-market rate concessional loans and grants into risk sharing mechanisms.

Actor	Components	Summary	Relevance
Development Finance Institutions (DFI)	Concessional loans, non-concessional loans, grants, common equity	• Provide grants, concessional loans, and other forms of direct development and climate financing. • Instrumental in mobilising private capital for Vietnam's transition through the provision of co-financing and de-risking supports, among others.	High
Bilateral partners	Concessional loans, non-concessional loans, grants, export credits	• Provide official development assistance (ODA) directly or through DFIs and multilateral concessional funds. • Provide other official flows (OOF) which include commercially oriented-grants and official bilateral transactions that have an export-facilitating purpose.	High

This is especially important for clean energy infrastructure projects which can pose significant perceived and actual political, technological, market and currency risks among others; they can also incur high upfront capital expenditure costs which are difficult to match with commercial cash flow requirements over a project's life cycle (see Section 1.2.3.). 1.2. Current state of low-carbon investment in Vietnam.

1.2. Current state of low-carbon investment in Vietnam

1.2.1. Investment needs

The decarbonisation of Vietnam's energy system is the country's central priority, accounting for over 70 per cent of investment needs. The importance of foreign capital is underscored by the gap between Vietnam's unconditional (15.8 per cent reduction below business as usual) and conditional (43.5 per cent) 2030 emissions reduction targets under its 2022 Nationally Determined Contribution (NDC). The latter is contingent on international support, of which finance is the central component. The energy sector is a particular priority, accounting for over 65 per cent of the country's emissions primarily through industrial, transport and residential end-use sectors (Socialist Republic of Vietnam [SRV] 2022; Danish Energy Agency 2022).

Of the total investment required to reach Vietnam's conditional 2030 target, 70.8 per cent must flow to the energy sector (SRV 2022). The IEA estimates that the Vietnamese government's target to have renewables account for 47 per cent of electricity generation by 2030 necessitates an approximate annual investment of over US$11 billion (IEA 2023). Other estimates place this figure at a similar level, underscoring the long-term scale of investment required. According to the World Bank, 80 per cent of the estimated US$81 billion in investment required between now and 2040 to reach net zero by 2050 must be directed to the energy transition (World Bank 2022). The need for attendant resilience and social measures lifts the overall energy investment figure far higher.

1.2.2. Private Investment Trends

To date, Vietnam's clean energy uptake has been largely driven by domestic and regional investment. However the scale of inflows required to realise stated emissions reduction targets will require a broadening of this investor base. Conversely, clean energy investment currently accounts for less than half of total energy investment - approximately 1.1 per cent of Vietnam's GDP, falling short of the investment needs detailed in Vietnam's NDC and PDP8 (IEA 2023b). To align with a net zero trajectory, clean energy investment must reach over 2 per cent of GDP (World Bank 2022).

Yet relative to other nations of the Association of Southeast Asian Nations (ASEAN), Vietnam has experienced a relatively large share of clean energy investment. This occurred particularly between 2019 and 2021 when attractive feed-in tariffs (FIT) offered through the FIT-1 and FIT-2 programmes led to investment inflows in the range of US$11.3 billion, briefly propelling Vietnam into becoming the world's seventh largest renewables market (OECD 2021).

This period has been a central driver of the country's region-leading 25-fold growth in renewables installed capacity. It has translated to Vietnam being the only country in ASEAN to exceed the global average for renewable electricity generation, reaching 11 per cent (Ember 2022).

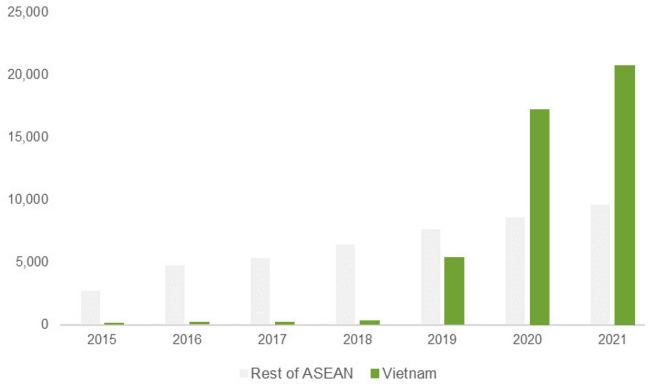


Figure 1. CO_2 emissions by sector in Vietnam: 2010 - 2020

Source: Author's analysis of data from IRENAStat (2023). Includes solar (PV and Concentrated), and offshore and onshore wind installed capacity only.

However, abundant untapped technical potential remains, and the Vietnamese government's Power Development Plan VIII (PDP8) targets a significant further increase in solar and wind capacity, with an aim of over 60 per cent of total installed capacity by 2050.

Significant transmission upgrades form a central part of this (see VNEEC 2023), but equally as critical to developing a greater share of capacity and translating this into generation in the short to medium term, will be further enhancement of the enabling environment to expand the scope and quantum of private foreign investment

Broadening the pool of investors into Vietnam's transition is particularly important. The sources of finance during Vietnam's capacity boom originated primarily from domestic and regional investors, concentrated among Southeast Asian and East Asian companies from Thailand, the Philippines, Singapore and Japan.

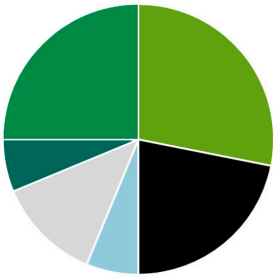


Figure 5a. Composition of financiers: Solar and wind

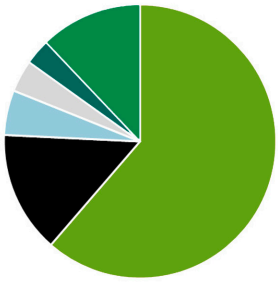


Figure 5b. Composition of project developers - Solar and wind

Source: Author's analysis of project-level data included in the Mekong Infrastructure Tracker (2023). Note: only operational solar and wind projects included in analysis.

As Figures 5a and 5b demonstrate, approximately 61 per cent of tracked solar and wind projects were initiated by domestic developers. Only around 6 per cent involved developers outside the region. Although the sample size for financial institution involvement is smaller, project level data show financiers outside the region were involved in 25 per cent of operational renewables projects, and solely in partnership structures with local or regional financial institutions. Domestic banks in particular have been a central source of capital for solar and wind power projects, accounting for US$3.6 billion in investments between 2018 and 2020 (UNDP 2022).

The presence of Australian companies in clean energy projects has to date been limited, although in 2022 Macquarie's Corio Generation announced a partnership with FECON, a Vietnamese company, to develop a 500 MW offshore wind farm in the Bà Rịa-Vũng Tàu Province.

As Vietnam sets out to achieve its climate targets, it is unlikely that domestic or regional financial capacity will be sufficient to initiate the volume of generation, transmission and storage infrastructure required.

There are numerous reasons why project development and financial flows to date have been relatively concentrated, including, among other factors, concerns with bankability issues and a lack of protections under Vietnam's power purchase agreements (PPAs), as well as a lack of understanding stemming from limited investor familiarity with the institutional context.

1.2.3. Public and Public-Private Investment Trends

As an emerging market economy, Vietnam faces a range of financial and non-financial obstacles to scaling its transition. Blended finance represents an important vehicle through which to de-risk low-carbon investments.

The role of public finance, provided bilaterally and through DFIs, is significant in driving emerging market transitions, particularly in low and lower-middle income economies where enmeshed barriers impede project bankability and private capital inflows.

These barriers include, but are not limited to:

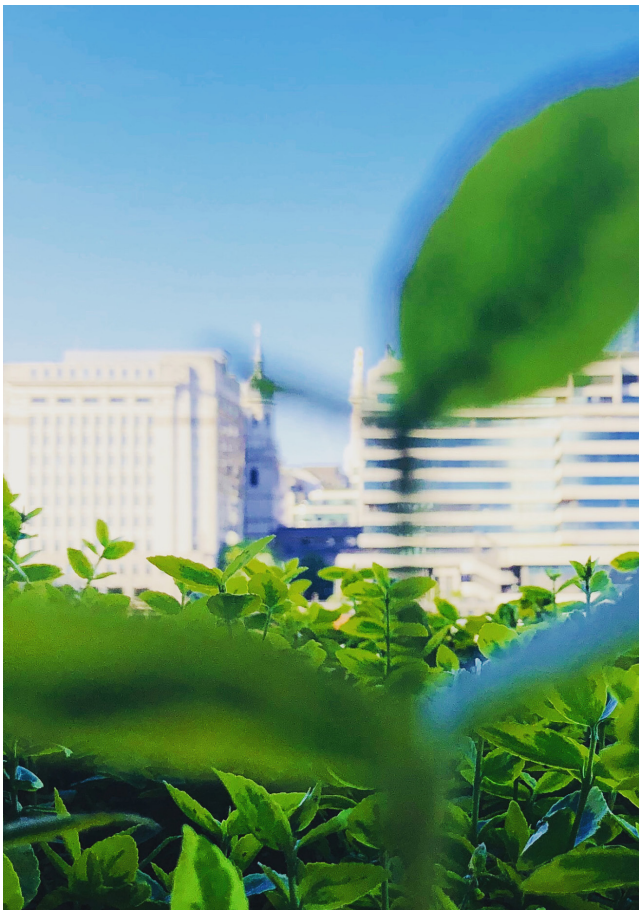
- high capital costs stemming from risk perceptions and a lack of familiarity with local contexts on behalf of international project developers, capital providers and credit rating agencies;
- economic feasibility issues relating to a mismatch between clean energy project return profiles in emerging economies and investor hurdle rates;
- underdeveloped climate information architecture and market transparency measures in host countries, and;
- unclear political, policy and regulatory signals relating to renewable energy targets.

De-risking through blended finance – a structuring mechanism that involves the strategic deployment of public capital to crowd-in private capital – is a commonly proposed solution to ameliorate the risk-return profile on emerging market low-carbon projects (Choi & Seiger 2020). The key sources of risk include political risks, policy and regulatory risks, offtake risks, currency risks and technology risks.

Vietnam has limited capacity to use domestic public financing for de-risking purposes. The country has a self-imposed debt-to-GDP ratio of 65 per cent. Their public debt level fell sharply from 58 per cent in 2018 to 38 per cent in 2022 (Ministry of Finance 2023). Although there is ample fiscal space, the public investment disbursement rate remains low due to public investment inefficiency and shortcomings in fiscal governance (World Bank 2023). The disbursement rate of public investment was 73.5 per cent in 2023. These conditions pose a structural challenge for mobilising finance for large scale projects requiring public finance, such as investment in clean energy infrastructure, transmission and coal retirement.

Blended finance cannot address all of the abovementioned obstacles. Other barriers such as private sector hurdle rates and certain institutional investors' minimum requirements on sovereign credit ratings also pose challenges to catalysing private investment. However, there is a clear role for the scaling of blended finance in Vietnam's transition. At present, Vietnam has been the third most active blended finance market in the ASEAN clean energy sector with a total of ten transactions, trailing Indonesia and Thailand (IEA 2023a). That Vietnam's generation growth outstrips these markets indicates that private investment alone has played a larger role thus far, likely through FDI.

The country's JETP (Climateworks Centre 2023) is expected to implicitly take the form of a structuring mechanism of this kind, also covering measures to enhance bankability and initiating institutional reforms. In this regard, it could play a pivotal role in establishing a national coordinating mechanism for blended transactions. The recently launched JETP resource mobilisation plan set out existing commitments from international donors. Grants only account for nearly 4 per cent of US$ bn 8.077 commitment, which might impact project bankability, given the country's limited capacity to use domestic funding for de-risking purposes. The Plan also set out a list of prioritised investments, with a focus on transmission, battery and storage, and offshore wind development in the near term.



Costs and Returns for Vietnam's Energy Transition

Among the economies of ASEAN, the average investment costs for solar PV in Vietnam are lowest, estimated at US$690 per kilowatt. Investment costs in wind, also cheapest in Vietnam along with Thailand, average around US$1,500 - 1,700 per kilowatt.

Vietnam also has the most competitive cost structures with regard to the levelised cost of electricity (LCOE) in ASEAN. For solar, this is approximately US$0.046 per kilowatt hour (kWh), and for onshore wind, it amounts to below US$0.05 per kWh. These figures are in comparison to the regional average of US$0.05-0.075 per kWh.

However, despite precipitous declines in renewables costs in Vietnam, the weighted average costs of capital (WACC), are a central determinant of LCOE. Comprising the aggregate cost of equity and debt, it is on average, more than double the cost faced by industrialised economies.

Furthermore, when denominated in VND rather than USD, the WACC is considerably higher, likely reflecting a currency risk premium. This poses additional cost issues for domestic financial provision, as depreciation relative to USD over time can increase the real cost of debt in particular. This indicates the role public finance can play in bringing down costs further and in line with those faced by industrialised economies.

	WACC (VND) - %	Expected return (VND) - %	WACC (USD) - %	Expected re-turn (USD) - %
Utility-scale Solar PV	10.1 - 13.6	12.5 - 15.5	7.5 - 10.5	12.0 - 15.0
Onshore Wind	9.6 - 13.1	12.0 - 15.0	7.0 - 10.0	11.0 - 14.5
Commercial and industrial-scale Solar	11.2 - 14.7	13.5 - 16.5	8.8 - 11.8	13.0 - 16.0

(Sources: IRENA & ASEAN Centre for Energy 2022; IEA 2023a).

While reliable and complete project-level data on public finance provision in Vietnam's transition is scarce, Figure 6 (at right) demonstrates that public multilateral and bilateral provisions have experienced high variations and have been overwhelmingly tilted toward non-renewables technical assistance, activities and projects.

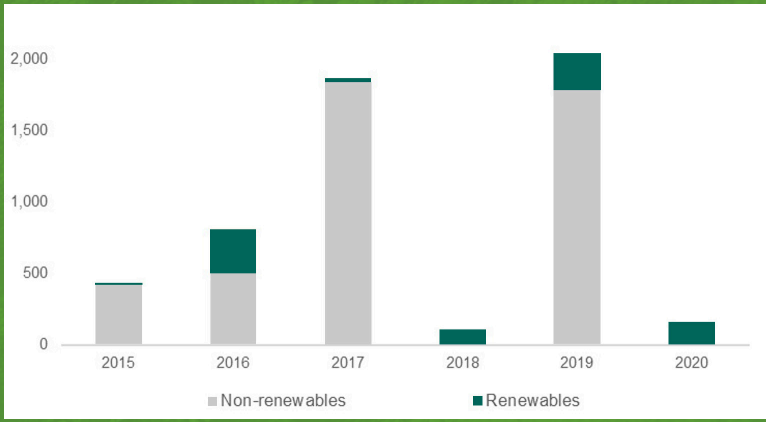


Figure 6. International public finance to Vietnam (US$m) - renewables vs. non-renewables
Source: IRENAStat (2022)

Additionally, the share of concessional loans and grants documented in international public flows into renewables has been relatively low.

	2015	2016	2017	2018	2019	2020
Grant	6.4	1.7	24.5	1.7	6.1	62.9
Concessional loan	-	175.1	-	-	27.1	9.9
Non-concessional loan	-	104.2	-	98.1	92.6	43.6
Commercial credit line *	-	-	-	-	100.0	-
Bond *	-	-	-	-	25.0	-
Common equity	-	20.8	-	6.0	-	44.9
Total	**6.4**	**301.8**	**24.5**	**105.8**	**250.8**	**161.3**

Figure 7. Breakdown of international public finance into renewables in Vietnam (US$m): 2015-2020
Source: IRENAStat (2022)
***Denotes commercial finance provided by DFIs and international governments to private enterprises in Vietnam and international organisations conducting renewable projects.**

The modest proportion of concessional flows may be explained by Vietnam's graduation to lower middle-income status, which has impacted eligibility for concessional finance (OECD 2019). There is, conversely, a substantial upside for bilateral and multilateral partners to enhance the provision of lower cost capital to support an equitable transition for Vietnam.

Deepening Australia's Export Finance for Vietnam's Transition

Export credit agencies can be influential and catalytic actors in enhancing bilateral FDI and trade relations, and there is scope for the Australian government to facilitate private sector investment in Vietnam's energy transition through targeted bilateral and syndicated loans.

There is a strong precedent and framework from which to enhance support: Export Finance Australia (EFA) is a partner of the Vietnam Climate Finance Framework (VCFF) under the Trilateral Infrastructure Partnership along with U.S. International Development Finance Corporation and the Japan Bank for International Cooperation; and has provided two separate lines of support since 2020 to support onshore wind development and electrification initiatives.

In 2021, EFA provided a US$32 million loan as part of a syndicated project finance package in partnership with the Asian Development Bank, the Japan International Cooperation Agency and private capital providers, to support the construction and operation of three wind farms in Vietnam's Quang Tri province. The project is expected to avoid approximately 162,430 tonnes of CO_2 emissions.

In 2022, EFA joined a syndicated loan partnership to support the manufacturing of electric public buses and Vietnam's first EV charging network.

The recent establishment of Australian Development Investments provides an opportunity for the strategic blending of concessional and non-concessional public capital to reduce capital costs, de-risking private Australian investment while deepening Australia's support for Vietnam's transition.

(Sources: EFA 2021; EFA 2022; EFA 2023).

2. Vietnam's sustainable investment framework

An enabling environment to attract low-carbon investment is far broader than a country's domestic sustainable finance market: It also encompasses institutional and sector-specific markers.

A range of often divergent factors influence sustainable investment range across contexts including the macroeconomic environment, institutional environment, natural conditions, exchange rate volatility, and land access laws, among numerous others (Keeley & Matsumoto 2018; Azarova & Jun 2021).

While no single definition or framework for an enabling environment to attract sustainable finance for Vietnam's low-carbon transition has been proposed, three broad dimensions, detailed in Figure 8, are particularly important to consider in Vietnam's push to enhance the domestic environment and incentivise a broader scope of investment from the region and beyond. These dimensions guide the structure of Section 2.

Area	Component	Summary
Institutional environment	Foreign investment governance	Strength of overarching framework and attendant provisions and incentives for clean energy investment.
	Sector-specific governance	Strength of sectoral governance framework with regard to providing procedural, operational and legal clarity.
	Sector-specific policy, regulation and incentives	Provision of policies, regulatory and incentive setting conducive to the promotion of long-term clean energy investment.
Climate policy framework	Alignment of climate targets	Breadth, ambition and alignment of climate targets and key climate policy documents.
	Other climate policies	Push and pull measures to establish policy and regulatory certainty and send positive investment signals.
Sustainable financial market settings	Market development	Measures to establish domestic public and private sustainable market maturity for low-carbon transition.
	Market transparency	Measures to promote the provision of a reliable climate-related information architecture

Figure 8. Key dimensions of the enabling sustainable finance environment for Vietnam's transition

2.1. Institutional Environment

2.1.1. Foreign investment governance

Vietnam's strong prioritisation toward attracting FDI has resulted in a robust and stable governance framework for this purpose.

The Foreign Investment Agency (FIA), Ministry of Planning and Investment (MPI) oversees investment promotion and facilitation in the country.

The FIA, among other functions, acts as a screening and facilitating point for inward investment. The local Department of Planning and Investment and Industrial Zone/ Export Processing Zone Management Board screens and approve foreign investment at provincial levels. It presides over the development and implementation of foreign investment policy and coordinates with relevant institutions to provide procedures and guidance with respect to any inward investment.

Foreign investment governance at domestic and provincial levels has markedly improved, with perceptions of policy certainty and political stability by international investors growing steadily between 2010 and 2022 (USAID & Vietnam Chamber of Commerce and Industry 2021, 2023).

Policies related to clean energy investment are growing, and measures underway to accelerate the development of green industrial sectors are important to scaling facility-level clean energy development.

The Law on Investment (Decree No. 31/2021/ ND-CP) and Public-Private Partnership Law constitute the most relevant legislation. No generalised limitation on foreign ownership in the renewable energy sector applies, and as an 'especially encouraged' sector, a range of incentives on foreign investment are available. These include import exemptions on project materials that cannot be domestically manufactured; a four-year corporate income tax exemption, along with a favourable tax rate thereafter; and exemptions on land lease fees (see Le 2023). As of 2023, MPI is in the process of developing a set of criteria aimed at accelerating the development of priority green industrial sectors backed by a set of incentives oriented toward international investors.

2.1.2. Sector-specific governance - renewable energy

The formulation and implementation of clean energy finance policy and legislation spans the Ministry of Industry and Trade (MOIT), Ministry of Finance, State Bank of Vietnam and MPI.

However MOIT is central in leading on the planning and implementation of clean energy activities, with approval on renewable energy projects under 50 MW and formulating key financing policies such as feed-in tariffs (FIT) and PPA. Further detail on energy governance is provided in Briefing Papers 1 and 2.

2.1.3. Sector-specific market and regulatory environment

To date, clean energy investment has been largely driven by attractive feed-in tariffs (FITs). While certain market risks have emerged concurrently, opportunities for commercial and industrial-scale investment are growing.

The role of economic incentives in attracting investment is well established. With regard to renewable energy uptake, a number of studies (CFLI 2021; OECD 2022) document

the significant correlation between foreign investment in clean energy and the application of FITs, an instrument through which long-term fixed price contracts for renewable power are offered to producers. EVN, the primary energy market operator in Vietnam which oversees transmission and distribution, is required under law to purchase the power generated by such projects at the stipulated FIT rate.

Vietnam's sizable renewable capacity growth has been spurred to a large degree by generous solar FITs (Do et al. 2020). The government's FITs for onshore and offshore wind, introduced in 2018 and extended to the end of 2023, have been similarly attractive, although system integration challenges and curtailment-related risks, particularly for utility-scale and rooftop solar, have also pushed up return requirements for investors (IEA 2023a).

Importantly for international investors, the introduction of a direct PPA (DPPA) program by the Vietnamese government is expected to recalibrate the dynamics of the energy market for foreign investment.

While the standard PPA puts EVN - as the primary energy market operator with a transmission and distribution monopoly - at the transactional centre, posing some investor risks (see Allens 2022), the DPPA program currently being piloted allows projects to sign PPAs directly with corporate offtakers and may provide significant opportunities for the expansion of C&I solar uptake across Vietnam's export-oriented industrial sectors.

2.2. Climate policy framework

2.2.1. Alignment of climate targets

The strength and integration of Vietnam's climate policy framework is highly important in sending long-term signals that can improve political and market risks for investors.

In emerging markets with rapid transition trajectories such as Vietnam, a strong climate policy framework that signals long-term and demonstrable ambition can help to mitigate market and political risks, thus contributing to reducing capital costs and broadening the investment pool.

As covered in this Briefing Paper along with Briefing Papers 1, 2 and 3, Vietnam has developed a broad set of key climate and climate-related targets, policy and strategic frameworks, including a conditional 2050 net zero target, the National Green Growth Strategy 2021-2030, the country's 2022 NDC accompanied by sub-targets under Decree No. 06/2022/ND-CP, PDP8, and the JETP platform through which Vietnam has committed to increasing the share of renewable capacity to 47 per cent by 2030, and is exploring coal retirement with international partners.

Additionally, Vietnam is a signatory to the Global Methane Pledge and the Global Coal to Clean Power Transition Statement. Together, these commitments represent a strong set of 'push' signals, particularly in the government's clean energy targets and mandates which are accompanied by strong institutional and cross-ministerial governance arrangements.

Vietnam has the opportunity to further align energy targets with climate objectives to provide consistent policy signals to the market.

The Vietnamese government has taken notable action to enhance coordination and alignment: Decision 2157/QD-TTg signed in December 2021, established a National Steering Committee on Climate Change to govern, coordinate and synchronise Vietnam's climate policies in the service of reaching net zero by 2050. However, there remains a disparity between the projected share of coal in power generation in PDP8 and the long-term net-zero target (Global Energy Monitor 2023).

2.2.2. Other climate policies

Vietnam's carbon pricing mechanism, set to be implemented in 2028, will be instrumental to enhancing investment signals toward low-carbon activities.

There is a positive correlation between explicit carbon pricing and greenfield investments in clean energy and low-carbon infrastructure. It is to the degree that increasing carbon prices by US$1 per tCO_2e can increase the number of low-carbon greenfield projects by nearly 1 per cent (OECD 2022).

In this regard, Vietnam's plan to introduce a mandatory domestic carbon market under Decree No. 06 can help to rebalance market and investment signals, and serve as a 'push' catalyst to incentivise FDI into both C&I and utility-scale clean energy projects. Additionally, it demonstrates a commitment to decarbonisation that acts to reduce policy and regulatory risks over the medium term.

The national carbon market will be piloted between 2025 and 2027, with commencement of operation targeted for 2028. As stipulated in the Law on

Environmental Protection 2020, the domestic carbon market includes activities of exchanging greenhouse gas emission quotas and carbon credits obtained from the domestic and international carbon credits exchange and offsetting mechanism following the provisions of laws and international treaties of which the Socialist Republic of Vietnam is a member.

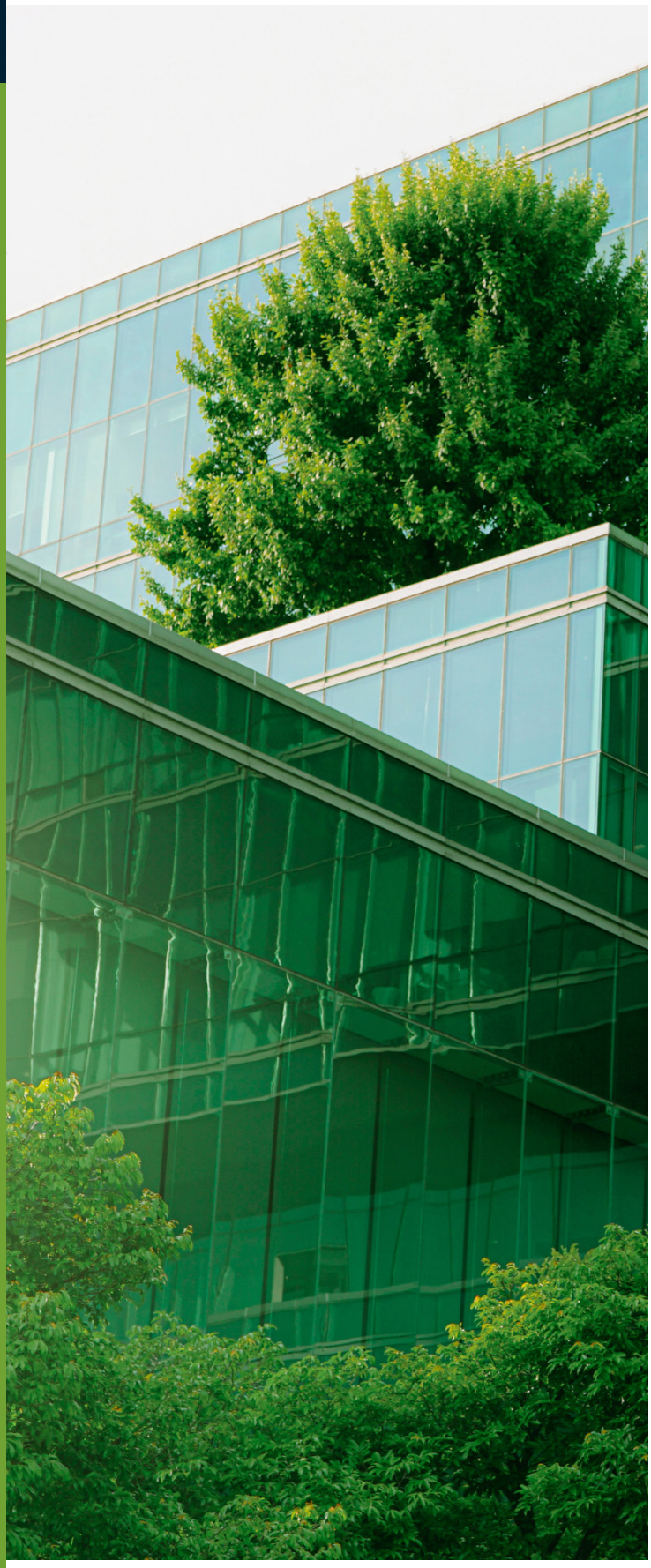
Projected medium term impacts of a Vietnamese carbon pricing mechanism, with regard to accelerating Vietnam's energy transition and delivering economic benefits, have been estimated as positive (see Chu et al. 2023). In the near term, carbon pricing policy should consider the impacts of the European Union's CBAM to ensure an adequate share of revenue is captured by the Vietnamese government across the CBAM's target sectors which are likely to expand over time.

2.3. Sustainable finance market settings

2.3.1. Market development

The development of sustainable financial markets in Vietnam has been modest but constitutes an important catalyst for the economy to broaden its investor base.

As with other ASEAN member states (with the exception of Singapore), the progress of sustainable financial market development in Vietnam has been mixed. A range of challenges have been cited, including resource constraints, incomplete information and lack of cohesive reporting standards, as well as a lack of enabling policies targeting the facilitation of sustainable market maturity.



Accessing equity – in particular for clean energy development – remains a challenge across the region, with stakeholders pointing to a constraint in equity available for early-stage project development.

A modest raft of sustainable finance policies have been introduced, including the Directive on Promotion of Green Growth issued by the State Bank of Vietnam (SBV); a green investment interest rate subsidy of 2.6 per cent provided by the Vietnam Environmental Protection Fund; and SBV's Circular No. 17/2022/TT-NHNN in 2022 which provides guidelines on environmental risk management in credit extension by local and and foreign financial institutions, SBV's action plan of the banking sector in promoting green growth. However, there remain other significant opportunities for the Vietnamese government to enhance 'push and pull' measures in the interest of incentivising domestic sustainable capital market mobilisation.

There is also a sizable opportunity to scale the utilisation of green debt, primarily through green bonds, to support the country's energy transition. At present, the depth of Vietnam's sustainable financial market is among the smallest of the ASEAN-5, and underperforms relative to comparable emerging market economies (WB & IFS 2022; IFC 2022).

Additionally, the Vietnamese government has not, at the time of writing, issued a sovereign green bond. Sovereign green bonds are an effective instrument to access relatively affordable debt capital for low-carbon projects and can be key to stimulating market activity, signalling intent and commitment to climate action, strengthening the government's track record with international investors, and enhancing capital market maturity.

While the Vietnamese government's public climate expenditure has been strongly adaptation-oriented to date (see UNDP & MPI 2022), sovereign green bonds could raise

valuable capital for mitigation activities. These could be utilised for direct investment or in concert with other forms of financing to incentivise clean energy projects. Proceeds could also be channelled through Vietnam's existing green finance mechanisms, the Vietnam Development Bank and Vietnam Environmental Protection Fund (see MPI & UNIDO 2019), to target demand and supply-side activation.

The institutional basis for issuing sovereign green bonds has been established (see ASEAN Capital Markets Forum 2022), and Vietnam's first onshore corporate green bond was issued in 2022. Additionally, due to the strong balance sheet and fiscal capacity of the Vietnamese government, the World Bank (2022) estimates that up to 1.3 per cent of GDP could be mobilised in sustainable debt without endangering public debt and the Vietnamese government's fiscal position over time.

Australian support for green bond issuances can encourage enhanced private sector institutional investment in Vietnam's transition, but must be coordinated.

Emerging markets such as Vietnam's often face obstacles to private sector participation, including, but not limited to, issues related to interoperability (see next section); a lack of familiarity with the track record of issuers; and developing financial markets which can, in turn, have an adverse bearing on risk perceptions and credit ratings.

In this regard, there is significant scope for support by the Australian government and private sector in coordination with multilateral fora to enable participation of international investors - particularly institutional investors that are major holders of bonds - in green bond issuances.

The first form that may be considered is the provision of insurance through guarantees on a sovereign issuance. Alongside direct investment in project finance vehicles, public guarantees have proven among the most effective tools for locking in private investment (OECD 2023). A range of different guarantees – including political risk guarantees or partial credit guarantees – can enhance the credit ratings of green bonds and, if well coordinated, broaden the sources of private sector participation.

For example, the Asian Development Bank in partnership with the Indian government's infrastructure fund, guaranteed a US$68 million green bond issuance for renewable energy, leading to a credit rating improvement from BBB to AA+ (Thuard et al. 2019).

The second form of support is taking a position through an anchoring or cornerstone investment in a green bond issuance. This can improve risk perceptions and demonstrate institutional confidence. There are opportunities for the Australian government, bilaterally and through multilateral organisations where it is a member, to pursue such measures to support the strengthening of green bond issuances in Vietnam. For example, Guarantco, of which Australia is a member, provided a US$50 million partial credit guarantee on Vietnam's first internationally-verified green bond last year, issued by EVN finance (Guarantco 2022).

Another emerging avenue is through the Indo-Pacific Net-Zero Transition bond series, being developed in partnership with the U.S., which aims to mobilise funding for the region's clean energy transition.

Concerted coordination with the Australian private sector, particularly institutional investors, will be key to this. This can ensure that guarantor mechanisms and anchoring interventions work to foster enhanced private investment into the opportunities presented through Vietnam's transition.

2.3.2. Market transparency measures

Enhanced market transparency measures are an important driver of sustainable financing inflows. Collaboration between Australia, Vietnam and ASEAN to strengthen interoperability is key.

Across ASEAN, measures to enhance market transparency related to low-carbon investments remain nascent. They can thus be an impediment to international investor participation (World Bank & IFS 2022). The development of a credible, verifiable and interoperable climate information architecture will create greater clarity for investors, and can contribute to the efficient pricing of transition risks and opportunities. In this regard, two areas - taxonomies and disclosures - are important to consider in Vietnam's transition.

Taxonomy and labelling

Within this context, a taxonomy refers to a system that categorises specific sustainable investments, generally at an activity and entity-level, to guide what constitutes a sustainable or low-carbon investment. Taxonomies assist investors' decision making by reducing information asymmetries and enabling an evaluation of whether an asset will support sustainability goals according to thresholds, benchmarks and/or principles.

While a range of taxonomies have been, or are under development across ASEAN - including the ASEAN Taxonomy, and domestic efforts across Indonesia, Singapore, Malaysia, and Thailand - Vietnam is yet to develop its own. The country's first certified green bond issuance last year was aligned with the ICMA Green Bond Framework.

The development of a domestic taxonomy that reflects the country's market environment and mitigation objectives is important to capture these benefits and send clear signals to investors about low-carbon investment priorities across the country.

A draft decree currently proposes the development of Vietnam's 'Green Bond Taxonomy' comprising an exhaustive list of 83 eligible project types. However, efforts to develop a taxonomy should prioritise interoperability, particularly with key investment partners. In this sense, there are opportunities for deepened collaboration between ASEAN, Australia (taxonomy under development), and Vietnam to ensure alignment across the region.

Sustainability and climate-related disclosures

The implementation of sustainability and climate-related disclosures has been fragmented across ASEAN, and Vietnam is no exception despite the importance of

capturing emerging physical and transition risks and opportunities. Although Circular No.155/2015/TTBTC requires public companies to produce an annual report disclosing their environmental impacts and objectives, Vietnam currently tracks at the lowest rate among ASEAN's largest economies in the adoption of existing global disclosure frameworks (Global Reporting Initiative & National University of Singapore 2022).

The recent introduction of the International Sustainability Standards Board's (ISSB) IFRS 1 and IFRS 2 standards, aims to cement a common, harmonised global baseline of sustainability and climate-related disclosures. They provide a blueprint and basis from which the Vietnamese government can enhance climate-related financial information to domestic and international investors alike.

This is particularly important for capital market actors, including banks and institutional investors, where such disclosures are critical inputs for risk management processes, also supporting the identification of transition opportunities.

The implementation of such a disclosure regime in Vietnam is likely to be highly challenging because emissions pathways across financial and real economy sectors remain largely undefined, and firm-level data complicates the identification, assessment and management of climate-related disclosures (GIZ 2023).

As such, increasing technical and administrative assistance is an area where the Australian government could significantly support the Vietnamese government and, in the longer term, Australian investors, as it embarks on the implementation of a mandatory disclosure regime and broader sustainable finance strategy.

3. Prospects for Australia-Vietnam Collaboration

Australian companies have the opportunities to benefit from Vietnam's sustainable finance prospects.

The briefing paper highlights Vietnam's attractive enabling environment for private investment in the country's transition, with commercial and industrial scale renewables for export-oriented firms representing a particular emerging opportunity along with a strong return profile across renewable technologies. Increasing climate commitments will create strong momentum to attract international investors.

As discussed, FDI constitutes the investment lever with the greatest potential due to robust governance, a strong incentive structure underpinning clean energy FDI, and the potential for export-oriented companies with transition plans to decarbonise energy-related emissions. The upcoming introduction of the DPPA mechanism will open up an important avenue for prospective and existing Australian investors and companies with net zero targets to develop distributed and C&I solar in particular.

The paper also highlighted several hurdles for investment, including policy uncertainties and certain technical financing constraints. Accordingly, as regional and international donors plan to scale up financing to Vietnam, Australian investors can engage with different blended financing instruments through multilateral donors such as ADB and World Bank, or through multi donor facilities such as JETP or the Private Infrastructure Development Group.

There is also a significant opportunity for the Australian government to play a more direct and proactive role in crowding in private sector investment through the establishment of a specialised Development Finance Institution that utilises public finance to ameliorate the risk profile of clean energy investments for Australian companies(ASFI, 2023). As it currently stands, a clear strategic mechanism that facilitates the deepening of bilateral low-carbon investment flows is unavailable, and the delineation of functions between EFA and ADI remains ambiguous.

The Australian and Vietnamese governments have taken strides to deepen climate cooperation, but there remains a significant opportunity to strengthen private sector engagement.

A number of live initiatives between Australia and Vietnam to strengthen economic ties and share capacity also prioritise support for, and private sector engagement with, the latter's energy transition.

Bilaterally, these include the Vietnam-Australia Enhanced Engagement Strategy, Australia-Vietnam Partnership for Economic Growth and work under Partnerships for Infrastructure. The Southeast Asia Energy Transition Partnership, of which the Department of Climate Change, Energy, Environment and Water is a member, and the Vietnam Climate Finance Framework under the Trilateral Infrastructure Partnership are key multilateral mechanisms.

As such, there is a strong institutional basis from which to strengthen public and private investment, and capacity building support in service of supporting Vietnam in its stated climate objectives, although there may be benefit in strengthening cross-government coordination between these initiatives and agencies, including EFA and ADI, to assist the cohesion and reinforcement of impact yielded through these growing interlinkages.

Despite strong momentum, the need for well coordinated support by the Australian government to both catalyse investment and encourage the development of Vietnam's sustainable finance market remains important. In particular the strategic and coordinated deployment of concessional capital can be influential in reducing the risk profile of investments while reducing capital costs.

Furthermore, taking a more active role in supporting green bond issuances and providing technical support to enhance market transparency and interoperability can be instrumental in laying the groundwork for longer term cross-border investment as Vietnam advances its ambitious climate agenda.

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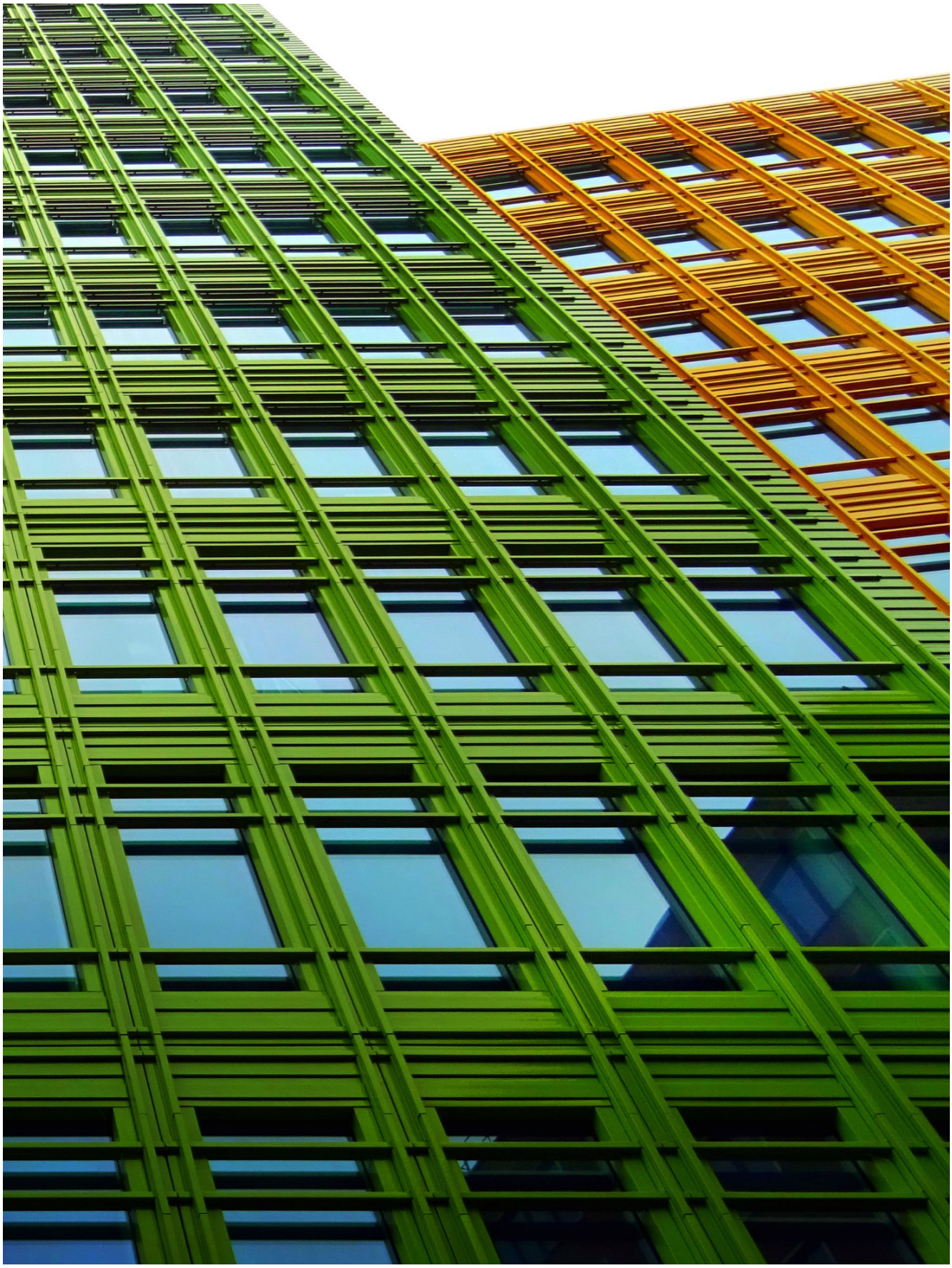

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