

VIETNAM'S TRADE STRUCTURE AND CHALLENGES FOR SUSTAINABLE GROWTH

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SUMMARY

- Vietnam has maintained a high economic growth rate led by external demand under export-oriented industrialization. In recent years, the country's primary export items have been shifting from low value-added products, such as sewing industry goods, to high value-added products, such as smartphones.
- Since 2009, an increasing number of companies have been transferring production to Vietnam, especially in the electronics industry, where Samsung Electronics is a notable example. This has created a trade structure under which Vietnam imports intermediate goods from China and exports final products to the US. The trend accelerated in the late 2010s due to the US-China trade conflict.
- For Vietnam to achieve sustainable growth, the challenge is to diversify the risks of a trade structure that relies on certain export items, and to stabilize the power supply.

Vietnam's economic growth has been supported by industrialization and an export-led trade structure. However, export-dependent economic growth is at risk of being adversely affected by external factors, such as a cooling global economy. This report provides an overview of Vietnam's economic strategy and its trade structure, and identifies challenges to the country's sustainable growth.

1. VIETNAM'S ECONOMIC GROWTH AND STRATEGY

The Vietnamese economy started transitioning to a "socialist-oriented market economy" under the Doi Moi economic reform policies launched in 1986. It has promoted industrialization and modernization in areas such as agriculture and consumer goods production since the 1990s. South Korea's Samsung Electronics started operating its first cell phone manufacturing plant in northern Vietnam in 2009, prompting other foreign companies to follow suit by transferring production to the country, and Vietnam's trade balance turned positive in 2012. Moreover, amidst the trade conflict between the US and China that has been intensifying since 2018, the US sanctions imposed on China have expedited the relocation of foreign companies' production bases from China to Vietnam. As a result, Vietnam has emerged as an alternative destination for exporting goods to the US. Vietnam's exports of industrial products as well as its attractiveness as an investment destination for foreign-capital companies have been growing, such that the foreign-invested sector has come to account for approximately 70% of exports in recent years¹.

Vietnam maintained a high GDP growth rate of around 6% year on year through 2019. Although the growth rate temporarily dropped to the 2% level from 2020 due to the COVID-19 pandemic, a V-shaped recovery was

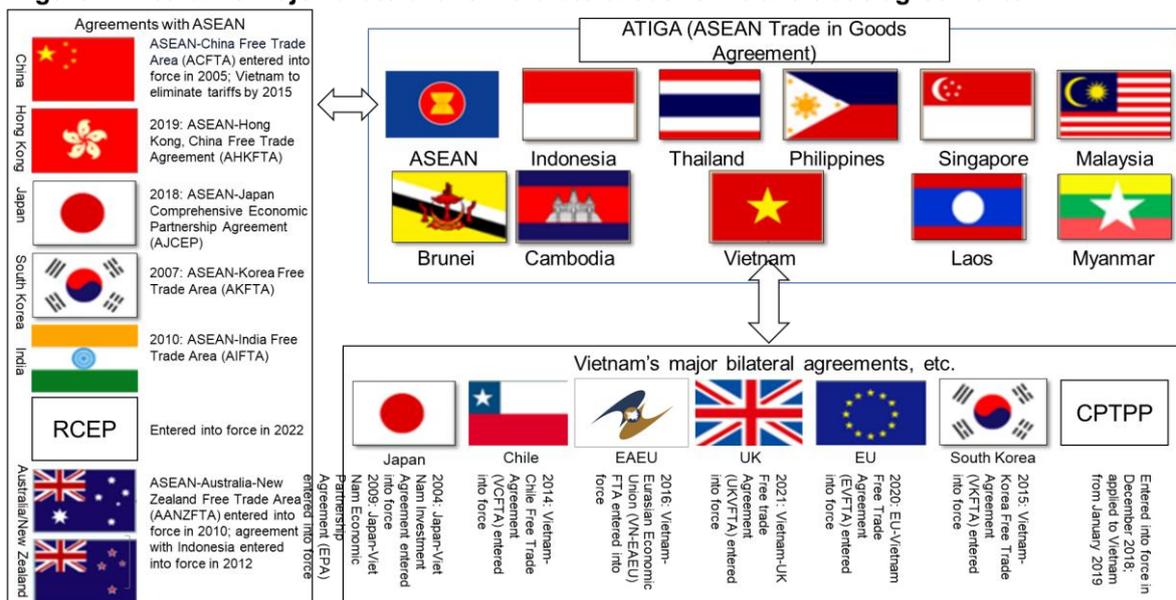
¹ Mai Fujita (2021), On the 13th National Congress of the Communist Party of Vietnam (2) Medium- and long-term development goals and direction, IDE Square [in Japanese], (accessed May 26, 2023)

achieved in 2022 when social restrictions were relaxed, and the country boasted one of the highest growth rates in Asia at 8.0%. However, the GDP growth rate for 2023 is expected to come in below the 6.5% target².

1-1 Trends in the area of economic partnership agreements

Vietnam's trade agreement with the US took effect in 2001. While the country does not have a free trade agreement (FTA) with the US, it has bilateral agreements and comprehensive economic partnership agreements with other countries and regions, as summarized in Figure 1. In recent years, through FTAs with the EU and the UK, where decarbonization-related regulations are stringent, Vietnam has been aiming to improve its international competitiveness by establishing high-quality production operations domestically that are compliant with such international rules³. The country's major exports to the EU and the UK include electronics products (including smartphones), coffee, sewing products, footwear, and furniture. For exports of these products, Vietnam will develop legislation to ensure that each step in the supply chain, from manufacturing to distribution, complies with strict environmental standards. Furthermore, Vietnam is preparing to satisfy the requirements of other countries that will adopt these environmental regulations in the future.

Figure 1: Vietnam's major bilateral and multilateral economic and trade agreements



Source: Compiled by MGSSI based on JETRO's global trade database, JBCI's report on the investment environment in Vietnam (Chapter 22: Trends in major industries and impact of FTAs), and other materials

1-2 Growth strategy to 2025 as set forth at the 13th National Congress

In Vietnam, the socio-economic development plan for the nation is presented every five years at the National Congress of the Communist Party of Vietnam, which evaluates the implementation of past policies and determines policy direction for the next five years. At the 13th National Party Congress held in 2021, the government set medium- and long-term goals for becoming a “developing country with a modern industry and upper-middle income level” by 2030 and a “developed country with high-income status” by 2045⁴, and set the target for the GDP growth rate for the five-year period from 2021 to 2025 at an average annual 6.5 to 7.0%⁵.

² According to interviews conducted by the author during a field survey on June 12-13, 2023, many respondents said they expect GDP growth to slow to 3-5% in 2023.

³ Based on a June 13, 2023 interview conducted at the Central Institute for Economic Management (CIEM), a research institute of the Ministry of Planning and Investment of Vietnam.

⁴ Vietnam has adopted a stance to shorten the time needed to transition from the level of a “middle-income country” to that of a “high-income developed country” as much as possible.

⁵ In order to become a “high-income country” without falling into the so-called “middle-income trap”, Vietnam must maintain a high GDP growth rate. The “middle-income country trap” refers to the situation in which a low-income emerging country, after becoming a

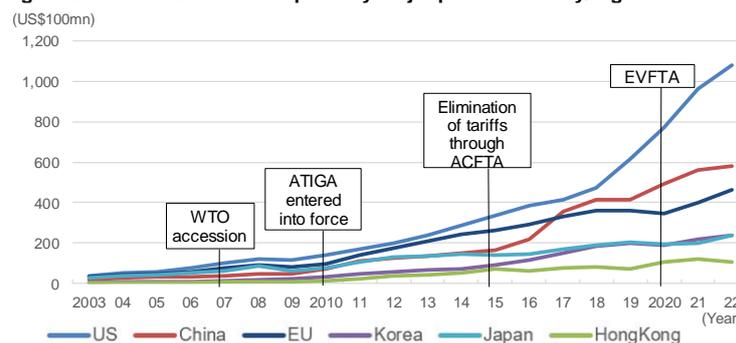
This reflects the government's recognition that Vietnam will not be able to become a “developed country with high-income status” by 2045 if it does not maintain a high GDP growth rate. In addition to expectations for digital technology, “prioritizing hi-tech projects that do not cause environmental pollution” was indicated as a direction of development⁶. Vietnam aims to advance its export-led industrialization through the enhancement of added-value industries.

2. TRADE STRUCTURE OF VIETNAM

2-1 Trends in Vietnam's exports and imports

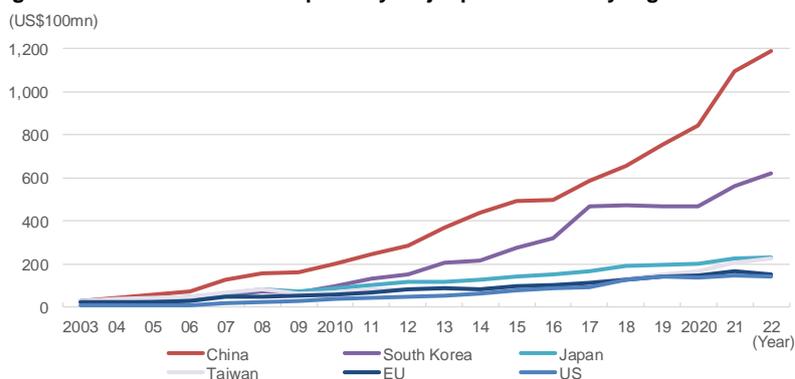
Vietnam's “socialist market economy” has enabled the government to maintain state ownership of electricity, telecommunications, and transportation sectors, while promoting joint ventures between state enterprises and foreign companies. After the country's accession to the WTO in 2007 and the conclusion of FTAs with other countries and regions, increasingly more foreign companies entered Vietnam, and that led to technology transfers and productivity enhancements. Initially, Vietnam's export items were mostly low value-added products, mainly from the sewing industry, but with the transfer of production of smartphones and other electronic devices to Vietnam, there has been a shift to higher value-added products. The absence of direct sanctions on Vietnam in the midst of the US-China trade conflict has also encouraged such transfers, and exports to the US and other countries increased up through 2022⁷ (Figure 2). Vietnam's dependence on exports as a percentage of its GDP was exceptionally high at 93.3% in 2021⁸. Imports are also on the rise, as raw materials used in the electronics and other industries are procured from China, South Korea, Japan, and other countries (Figure 3).

Figure 2: Vietnam's value of exports by major partner country/region



Source: Compiled by MGSSI based on the IMF's Direction of Trade Statistics (DOTS)

Figure 3: Vietnam's value of imports by major partner country/region



Source: Compiled by MGSSI based on the IMF's Direction of Trade Statistics (DOTS)

middle-income country, has difficulty in rising to a developed country (high-income country) and takes several decades to do so. For more information on the “middle-income country trap” in Southeast Asia, see “The Middle Income Trap from a China and ASEAN Perspective” by Tran Van Tho and Shunji Karikomi, Tokyo, Keisou Shobo, 2019.

⁶ Shozo Sakata (2021), Results of the 13th Party Congress of the Communist Party of Vietnam (3) Direction of economic development, IDE Square [in Japanese] (accessed May 26, 2023)

⁷ Figures are for the full year; exports declined from the fourth quarter of 2022 onward.

⁸ Based on data on the World Bank website (accessed June 29, 2023)

The steady increase in imports from South Korea, as shown in Figure 3, is attributable to the establishment of Samsung Electronics and LG smartphone production plants in Vietnam, and the local production by those companies has led to an increase in imports of intermediate goods. The impact of Samsung Electronics on Vietnam's imports and exports is particularly significant. The number of Vietnamese subsidiaries operating under Samsung Electronics increased to four in 2016, and the total value of Samsung Electronics sales in Vietnam has continued to represent about 20% of Vietnam's total exports in recent years (Figure 4)⁹.

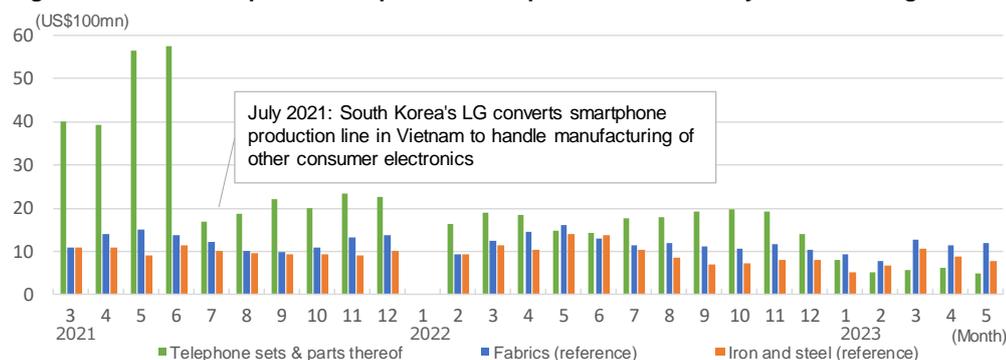
Figure 4: Sales of 4 Samsung Electronics Vietnamese subsidiaries as a percentage of Vietnam's total value of exports



Source: Compiled by MGSSI based on data of the General Statistics Office of Vietnam and Samsung Electronics annual report

Thus, Vietnam's proportion of smartphone-related exports and imports is high, and the country's economic situation can be said to be easily influenced by specific industry trends. In the first half of 2022, both imports and exports reached record highs on a recovery in demand resulting from the easing of pandemic-related restrictions, but in the second half of the year, the growth of imports and exports slowed down due to sluggish external demand caused by the economic slowdown accompanying global inflation¹⁰. Worth noting is that the import value of "telephone sets and parts thereof" has been declining sharply since July 2021 (Figure 5). In April 2021, LG of South Korea announced that it would withdraw from the smartphone business at the end of July of the same year, and it is believed this was inexplicably linked to its decision to end smartphone handset production in Vietnam and shift production lines to cell phone components and other consumer electronics¹¹. In addition, with overall smartphone shipments declining worldwide¹², Samsung Electronics is scaling back production in Vietnam¹³ to diversify business risk against external factors beyond its control, such as contagious diseases.

Figure 5: Vietnam's imports of telephone sets & parts thereof and key intermediate goods



Note: Import statistics for January 2021 were not disclosed.

Source: Compiled by MGSSI based on data of the Vietnamese General Department of Customs

⁹ Samsung Electronics has four subsidiaries in Vietnam: Samsung Electronics Vietnam Thai Nguyen Co. Ltd., Samsung Electronics Vietnam Co., Samsung Electronics HCMC CE Complex Co., Ltd., and Samsung Display Vietnam Co., Ltd. The sales figures in Figure 4 were calculated based on an exchange rate of US\$1 to 1,281.10 Korean won.

¹⁰ JETRO Business Tanshin (2023), [Trade volume in 2022 hits record high, but slows down in second half \(Vietnam\)](#) [in Japanese] (accessed June 5, 2023)

¹¹ At the time, LG's production operations in Vietnam accounted for half of its global smartphone output.

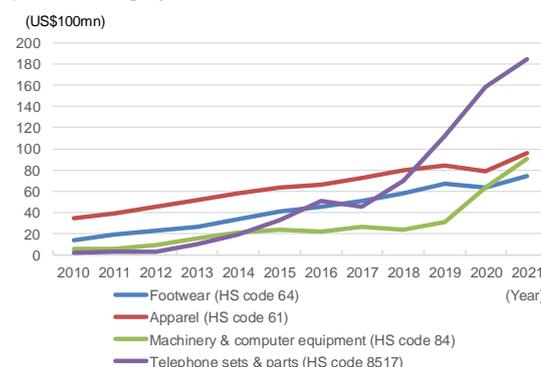
¹² Total global smartphone shipments fell 18.3% YoY in Q4 2022, and Samsung, which was the leader in total shipments for the entire year, was overtaken by Apple. ["Smartphone Shipments Suffer the Largest-Ever Decline with 18.3% Drop in the Holiday Quarter and a 11.3% Decline in 2022, According to IDC Tracker"](#), IDC, (accessed June 28, 2023)

¹³ ETNews (November 4, 2022) ["Samsung Phones, Cutting Production in Vietnam by 40%"](#) (accessed June 28, 2023). Samsung Electronics had been producing nearly 60% of its smartphones in Vietnam until 2021, but it is dispersing production to other parts of Asia and South America, and plans to decrease production in Vietnam to nearly 40% of the total by the end of 2023.

2-2. Exports to the US by product category

In 2001, Vietnam entered into a bilateral trade agreement with the US, its largest export partner, then the US granted it the designation of permanent normal trade relations (PNTR) as part of Vietnam's accession to the WTO in 2007¹⁴. The country's main export products are textiles and footwear, and the electronics industry has been marking conspicuous growth in terms of the export value of "telephone sets and parts thereof" since 2018, driven by increased exports of smartphones (Figure 6). Vietnam's trade tends to be influenced by the US economy, and the prospect of a US recession in 2023 is a concern for the impact on its exports to the US.

Figure 6: Vietnam's value of exports to the US by major product category

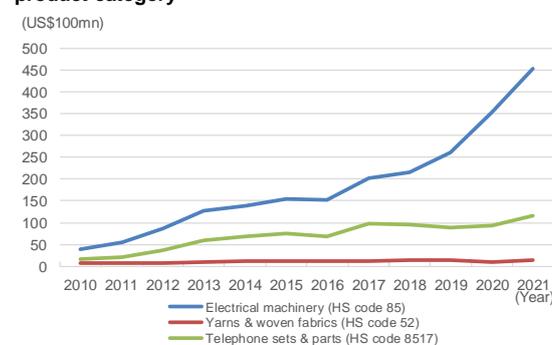


Source: Compiled by MGSSI based on the UN's Comtrade database

2-3 Imports from China by product category

Vietnam's trade with China, its largest import partner, has expanded since the ASEAN-China free trade agreement eliminated tariffs in 2015. The relocation of production bases by electronics-related companies, such as Samsung Electronics (South Korea) and Apple (US), to northern Vietnam also contributed to the increase in imports of intermediate goods for "telephone sets and parts thereof" from China (Figure 7). As Vietnam is not a resource-rich country, the procurement of raw materials is essential. Furthermore, the country has not developed basic industries for the manufacturing sector, so the option of not importing raw materials from China is not a realistic one¹⁵.

Figure 7: Vietnam's value of imports from China by major product category



Source: Compiled by MGSSI based on data of UN Comtrade and the General Statistics Office of Vietnam

2-4. Electricity shortage issue seen as a risk to watch

There have been reports of severe power shortages in Vietnam, starting from around late May 2023. In northern Vietnam, where many smartphone manufacturing plants are located, hydroelectric power generation is the main source of electricity. However, while demand for electricity increased, the El Niño phenomenon caused intense heat and reduced precipitation, leading to a drop in the water level in dams and rolling power outages in early June. Manufacturing companies in the north were forced to cut power every other day, or every few days, and adjust production accordingly. Failure to quickly resolve this issue will increase the likelihood of an exodus of foreign companies that are currently operating in Vietnam, and a contraction in the country's manufacturing sector could have a significant impact on the nation's trade structure and economic growth. Although the National Power Development Plan for 2021-2030 (known more commonly as the Power Development Plan 8, or PDP8) was approved in May, two years later than originally scheduled, it will not result in a sweeping solution to the problem unless the government aggressively promotes measures such as gas power generation using domestically produced natural gas, which is a component included in the plan¹⁶. The electricity shortage issue needs to be closely monitored as a long-term risk for doing business in Vietnam.

¹⁴ Vietnam does not have a free trade agreement with the US.

¹⁵ In the on-site interviews conducted on June 12-13, many respondents indicated that Vietnam needs to import intermediate goods because it has not developed basic industries for the manufacturing sector.

¹⁶ Vietnam, which has announced its intention to achieve carbon neutrality by 2050, plans to reduce use of fossil fuels and transition to hydrogen, but during this transition period, thermal power generation using domestically produced natural gas and imported LNG will be used as a temporary power source. The Block B project, a gas field for domestic natural gas production, is positioned as an important project for solving the electricity shortage problem through stable energy supply and for supporting the energy transition going forward.

3. CONCLUSION

Vietnam aims to achieve a high GDP growth rate to become a “developed country with high-income status” by 2045, and to transition to high value-added industries through expanded trade agreements. In recent years, foreign companies have shifted production from China to Vietnam for reasons such as to avert risk in consideration of US economic sanctions against China, and growth has been conspicuous in the high value-added industries, particularly the electronics industry. As for exports to the US, there has been a marked increase in shipments of “telephone sets and parts”, which, along with machinery, had been key to Vietnam's economic growth.

However, as described in this report, a trade structure that is overly dependent on specific products such as smartphones is risky. By way of illustration, consider the example of smartphone production by Samsung Electronics and LG; changes in the strategies of individual companies can significantly affect the trade of an entire country. To avoid this situation and ensure sustainable economic growth, it is necessary to diversify the risks of a trade structure that depends on specific export items. The other major issue is the electricity shortages in Vietnam, and domestic natural gas production and other solutions are positioned as important for alleviating this problem. Actions to resolve these issues are urgently needed.