

Wiemann, Jürgen et al.

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## Vietnam: the 150th WTO-member, implications for industrial policy and export promotion

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Vietnam – the 150th WTO-member  
Implications for industrial policy and export promotion

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## Vietnam – the 150th WTO-member

Implications for industrial policy and export promotion

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## Preface

The present study aims at identifying the key issues in the field of industrial policies and export promotion where present policies and practices of Vietnam may conflict with the rules and agreements of the WTO. Vietnam applied for WTO membership in 1995, exactly when the WTO succeeded the GATT Secretariat with a wider package of rules and agreements that had been negotiated during the Uruguay Round 1986–1994. It took some time until developing countries, incited by a rising tide of worldwide criticism of civil society groups and heterodox economists, began to question the implications of the new agreements and commitments that had come out of the Uruguay Round in GATT, for their capacity to stimulate industrial development with a mix of infant-industry protection, selective government support and export subsidies. Meanwhile, the narrowing of *policy space* has become one of the contentious issues in the debate about the development impact of the present multilateral trade negotiations, the Doha Development Round.

To do a study on the implications of Vietnam's WTO membership on its industrial policy options and export promotion capacity was motivated by the observation that outside the small circle of Vietnamese trade negotiators there was very little information and awareness of the implications of WTO membership on Vietnam's economic policies and its capacity to improve the competitiveness of domestic industries in the globalizing economy. This impression was gained during several WTO workshops that had been organized jointly by the German aid agency DSE/InWEnt and the NCIEC in Hanoi for Vietnamese government officials, representatives of government agencies, of business associations and universities, to which I had been invited to present the WTO obligations for an accession country like Vietnam.

Taking, in 2004, a team of young researchers from the postgraduate training course of the German Development Institute for a field study of two and a half months to Vietnam, offered the opportunity to gather more information on Vietnam's economy and to conduct a wide range of interviews with government officials, state agencies in the field of industrial policies and export promotion, business representatives, aid agencies and research institutions on their experience with industrial policies and export promotion and their expectations on the implications of WTO membership. The results of the field study were presented in Hanoi at the end of the field research, and again at more workshops in Hanoi and Berlin in

2004 and 2005, organized by InWEnt, the Friedrich-Ebert-Foundation (FES) and the Konrad-Adenauer-Foundation (KAS). In the name of the team I wish to thank once again all institutions and companies which have supported the study by giving interviews and providing insights into their enterprises and institutions as well as offering additional written information. We are especially grateful for the hospitality and professional cooperation we experienced at the Central Institute for Economic Management (CIEM) in Hanoi. Of course, the responsibility for errors and misunderstandings remains with the German Development Institute (DIE) Team.

After the team had been dissolved at the end of the training course in May 2004, it took more time than expected to finalize the study for publication due to several other obligations of the team leader in his capacity as deputy director of the German Development Institute. However, the delay provided more time for reflection on the fundamental question whether the new wave of books and papers criticising the unfairness of the WTO processes for developing countries would lead to a different assessment of Vietnam's decision to join the WTO.

The answer is a cautious "no". WTO membership will provide the framework for the still ongoing economic reforms and prevent Vietnam's economic policy makers from slowing down the process of economic reforms that are still required for making Vietnam fit for international competition both at home and on export markets. The WTO itself does not prosecute a member country that does not fully comply with a WTO agreement. As long as Vietnam maintains the present good relationship with its major trading partners and is able to make them understand why the full implementation of the WTO agenda will take some more time, there should be no reason for taking Vietnam "to court" for non-compliance. Vietnam's experience with complying with the full set of WTO rules and agreements will be carefully watched by the critics of the system, and this should be a guarantee for fair and flexible treatment.

From a broader perspective, one could even argue that Vietnam has benefited already, even as a non-member, indirectly from the past rounds of multilateral trade negotiations und the GATT. Vietnam's rapid economic recovery since the beginning of economic reforms has been facilitated by the openness of export markets. This favourable international environment is a result of the successful multilateral rounds of trade negotiations under the GATT which have led to a world-wide reduction of tariffs and other import barriers, especially in the field of industrial products. Trade liberalization together with the dramatic decline in costs of international trans-



port and communication had triggered off the process of economic globalization. The most important aspect of this process is that companies all over the world have gained experience with establishing production capacities overseas and organizing international trade within international production networks and supply chains. They were eager to find new locations like Vietnam for their international production and marketing strategies.

Thus, it seems fair from a global viewpoint that Vietnam gives up its free-rider position and becomes a WTO member in its own right. As a WTO member committed to complete its economic reform programme, Vietnam will become even more attractive for foreign investors. The task for Vietnam's industrial policy makers will now be to broaden the industrial base by helping domestic industrial enterprises to improve their capacity to link up to these international supply chains and become ancillary suppliers to foreign investors or direct exporters.

Vietnam's accession to the WTO which has been approved by the General Council on 7 November 2006, is not only a milestone for Vietnam, it is important for the multilateral trading system as well. This was expressed by the WTO Director-General Pascal Lamy, at the General Council Meeting when he said: "*WTO membership is not only important for Vietnam, but for the organization too. With Vietnam joining in, we demonstrate to the world that the multilateral trading system continues to show its uniqueness, comprehensiveness and attractiveness.*" Vietnam's willingness to accept the obligations of WTO membership should embarrass the incumbents who have not been able, in July 2006, to agree on a compromise which would bring the Doha Development Round to a successful conclusion. As a WTO member, Vietnam will now be able to demand from the major players in the WTO that they contribute their share to the functioning of the system and to concluding the suspended round in a way that will take account of the special interests of the different groups of developing countries.

Bonn, November 2006

Jürgen Wiemann



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## Abbreviations

AEC	Asean Econom Community
APEC	Asia-Pacific Economic Cooperation
ASEAN	Association of South-East Asian Nations
AFTA	ASEAN-Free Trade Area
CEPT	Common Effective Preferential Tariff Scheme
CIEM	Central Institute for Economic Management
CPV	Communist Party Vietnam
CVA	Customs Valuation Agreement
DDA	Doha Development Agenda
DSE	Deutsche Stiftung für Internationale Entwicklung
ERP	Effective rate of protection
EPZ	Export Processing Zones
EU	European Union
FDI	Foreign Direct Investment
FIE	Foreign invested enterprises
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
HS	Harmonised System
IAP	Individual Action Plans
ILO	International Labour Organization
IMF	International Monetary Fund
InWEnt	Internationale Weiterbildung und Entwicklung
IP	Intellectual Property
IPR	Intellectual Property Rights
ISO	International Standards Organization
ITPC	Investment and Trade Promotion Center
ME	Market Economy
MFN	Most favoured nation
MOST	Ministry of Science and Technology



MPI	Ministry of Planning and Investment
MUTRAP	Multilateral Trade Policy Assistance Programme
NCIEC	National Committee for International Economic Cooperation
NGO(s)	Non-governmental Organization(s)
NICs	Newly Industrializing Countries
NME	Non-market Economy
NOIP	National Office for Intellectual Property
NTB	Non-tariff barriers to trade
OECD	Organisation for Economic Co-operation and Development
QR	Quantitative restrictions
R&D	Research and Development
SCM	Subsidies and Countervailing Measures (WTO Agreement)
SDT	Special and Differential Treatment
SME	Small and medium enterprise
SOE	State-owned enterprise
SPS	Sanitary and Phytosanitary Measures
STAMEQ	Standards and Quality
TBT	Technical Barriers to Trade
TCVN	Vietnamese Standards
TPO	Trade Promoting Organizations
TRIMs	Trade-Related Investment Measures
TRIPS	Trade-Related Aspects of Intellectual Property Rights
TRTA	Trade-Related Technical Assistance
UNIDO	United Nations Industrial Development Organization
UPOV	International Union for the Protection of New Varieties of Plants
US BTA	United States-Vietnam Bilateral Trade Agreement
VAT	Value Added Tax
VCCI	Vietnam Chamber of Commerce and Industry
VIPA	The Vietnam Intellectual Property Association
VND	Vietnamese Dong

VSC	Vietnam Standard Centre
WIPO	World Intellectual Property Organization
WTO	World Trade Organization



## Summary

Since the beginning of its economic reform programme (*doi moi*) in 1986, Vietnam has made an astonishingly great leap forward. However, export success was mainly based on increasing commodity exports and on venturing into new export markets for agricultural and fish products. In addition, foreign enterprises were invited to tap Vietnam's relatively cheap, yet well educated and highly motivated workforce for their strategies of global sourcing. This commodity-based export strategy, however, will not allow maintaining the high growth rates of the early years of market reforms. The decline of coffee prices has revealed already that there are limits to growth for commodity exports even from one country only. Therefore, Vietnam, like other countries in the region, will have to diversify its exports towards manufactured goods and catch up with the more advanced competitors. In order to prepare for the shift towards export diversification and to get a better and secured access to the major export markets, Vietnam joined the ASEAN (Association of South-East Asian Nations), signed a bilateral trade agreement with the United States and applied for World Trade Organization (WTO) membership.

WTO membership will be an important prerequisite for the strategy of export diversification: Firstly, because access to export markets of all WTO member states will be secured by the most-favoured nation (MFN) principle; secondly, because Vietnam's import policy and economic policy in general will be subject to the multilateral rules of the WTO and will thereby become more stable, predictable and transparent; thirdly, WTO rules and agreements will provide the framework for reforming Vietnam's economic and trade-related legislation and institutions. Thus, as a WTO member country, Vietnam will not only gain attractiveness for foreign investors, but also national entrepreneurs will be encouraged to invest in new plants and machines if they can rely on the stability of the legal framework and economic policies. However, there are reasons for taking a more sober look at the implications WTO membership will have for Vietnam's ambitions to promote industrial development and new exports.

When Vietnam submitted its application for WTO membership in 1995, the WTO had just been established as the successor of the General Agreement on Tariffs and Trade (GATT). As a result of the Uruguay Round in GATT, the WTO is now covering new areas like services and intellectual

property rights, and many of the old rules of the GATT, including the dispute settlement system, have been strengthened. Developing countries had more actively negotiated in the Uruguay Round than in previous GATT Rounds, offering own concessions, and they had accepted that the new agreements were binding their own policies and activities in the new areas, in return for concessions from the developed member countries. Only after some time, the implications for developing countries of the new rules and agreements of the WTO became visible and the real costs of some of the new agreements were calculated. This provoked a rising tide of criticism of the unfair bargain the developing countries had achieved in the Uruguay Round, and the new Round in the WTO, launched in Doha, Qatar, in 2001, was labelled *Development Round* to signal to developing countries that this time their concern about the unfairness of the system and the repercussions of some of the new disciplines would be taken seriously. The debate on the developmental impact of the WTO system focuses on the narrowing of the *policy space* for developing countries resulting from the discipline that the new agreements impose on trade-related domestic policies. Can the latecomers like Vietnam apply the same active and selective industrial policies that the successful East Asian Newly Industrializing Countries (NICs) used in their early phase of industrial development and export diversification? And if not, is the narrowing of policy space good or bad for economic development and poverty alleviation?

Sound macroeconomic policies encouraging savings and investment, open markets stimulating learning and adopting modern technologies, production and marketing concepts will always be the key to successful development. In addition to that, the advocates of modern industrial policy see a need for government support to private firms that take major risks when they venture into unknown territory, i. e. importing and adapting new technologies or venturing into a new export activity and getting an inroad into a new export market. Every country will have to find out what will be the most appropriate mix of macroeconomic and industrial policies to promote economic development most effectively and in a way that helps to reduce poverty and to achieve the Millennium Development Goals.

The debate on *policy space* under the WTO is relevant for Vietnam because the Government of Vietnam has applied and is still applying a number of industrial and export promotion policies that will no longer be allowed under the WTO. Will that be an undue price for the vague promise of more secure access to export markets and increasing inflow of foreign

investment? After a brief summary of Vietnam's transition to an open economy, the present study gives an overview of the new rules and agreements of the WTO which confine the industrial policy space in general, followed by an introduction into the actual debate on industrial policy and the developmental state. The consequences for Vietnam will be to continue its economic reform programme and to creatively apply positive measures for encouraging the restructuring of industry so that the domestic industry will become technologically more competent and able to find new export markets directly or indirectly by becoming efficient suppliers to the foreign companies manufacturing in Vietnam for the world markets.

With respect to time and capacity limits, the study focuses on the challenges for industrial policy and export promotion. The implications of WTO membership for agriculture and services could not be included in this study. The study illuminates five topics related to Vietnam's industrial policy and export promotion against the background of its forthcoming WTO accession and multilateral economic integration. Taking into account the perceptions of interview partners on the level of government ministries and agencies, intermediate institutions like business associations and on the level of individual enterprises, the following conclusions can be drawn:

**Import liberalisation** will have different consequences for the different industries and types of enterprises. Compared to the other WTO issues affecting industry policy, the reduction of tariffs seems to be a minor problem for Vietnam, but still a major problem for some industries. Vietnam's average tariff level is comparatively moderate though at the higher end of its neighbouring states, which are already WTO members. However, some industries are still protected by very high tariff rates, e. g. the automotive and the textiles and garment industries. Therefore, the challenge regarding import liberalisation will be to harmonise and simplify the current tariff system and thereby to remove these high protection levels. Hence, all enterprises will have to prepare for stiffer competition on the domestic market. Private small and medium enterprises (SMEs) may be flexible enough to meet this challenge and will face less problems than the larger and often highly protected state owned enterprises (SOEs). The Vietnamese government would be well advised to build on the flexibility of SMEs and strengthen their capacity for growth and for exporting. With respect to import liberalisation, the most important task will be the establishment of transparent and reliable trade policies with simplified and predictable

customs valuation and transparent regulations for imports and exports. This could be achieved by reducing and streamlining tariff rates for different product categories required for WTO accession, which would reduce the potential for arbitrary classification of imported goods and for informal extra-payments. In addition to that, concerns that tariff reductions will lead to major losses of government revenues may not be justified. With lower tariff rates, imports to Vietnam may be growing so fast that the lower rates may be compensated by larger volumes of imported goods. Lower tariffs would also reduce the incentives for circumvention of customs through smuggling, thus more imports would be officially declared and generate additional tariff revenues.

The need of phasing out the **localization policy** will require some important changes in industrial policy. The Trade-Related Investment Measures (TRIMs) Agreement requires governments of WTO member countries to phase out all measures distorting foreign trade from its “natural” level and patterns. This obligation refers especially to *local content policies*, which many developing countries have implemented until recently, mainly for automotive industries. Following their example, Vietnam is trying to develop an integrated automotive industry by stimulating *backward linkages* of the automobile assembly plants and encouraging the development of local ancillary industries. The major challenge for Vietnam after WTO accession will be to establish and promote competitive ancillary industries without forced localisation policies, while competition with foreign suppliers will increase at the same time. The TRIMs Agreement clearly prohibits making the licensing of a foreign investment conditional upon the acceptance of certain performance requirements, like local content requirements, that are no longer allowed under the TRIMs Agreement. Moreover, the WTO Dispute Settlement decision on Indonesia’s national car programme shows that not only direct but even indirect measures to encourage localisation like variable duty rates and tax incentives are considered trade-related investment measures covered by the TRIMs Agreement. Therefore, the Vietnamese government will have to develop other strategies for encouraging and supporting the development of a national ancillary industry and lifting it to the technology and quality level required by the automobile assembly plants. Then these enterprises would purchase more domestic inputs out of their own interest and without being forced to do so by government regulations and restrictions.

The **enforcement of intellectual property rights** (IPRs: patents, copy-

rights, trademarks etc.) is an additional challenge for Vietnam and its industrial policy arising from global economic integration. In the Bilateral Trade Agreement with the United States (US BTA), Vietnam has already accepted to respect IPRs and to prevent infringements more effectively. The WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) will make this only a general obligation to respect IPRs of all other WTO member states. Even if the Vietnamese patent and copyright legislation has already been adjusted in view of the international requirements, there is still a huge gap between legislation and effective enforcement of IPRs on the micro level. Many Vietnamese are not aware yet of the meaning of intellectual property rights, and awareness is rising only slowly. Moreover, even Vietnamese experts state that the institutions, which are to enforce IPRs, do not yet work satisfactorily. There are problems of communication and co-ordination between the different institutions involved, and training for the staff of these Organizations and for enterprises is lacking. Thus, the main challenges for Vietnam in the field of IPRs are to complete the adoption of TRIPS obligations in national legislation, to improve the work and co-ordination of the various enforcement institutions, and, last but not least, to raise awareness on IPRs among the Vietnamese people. Technology policy will become an increasingly important aspect of Vietnam's industrial policy. The enforcement of IPRs will not only make the country more attractive for foreign direct investment (FDI), it should also encourage domestic innovation and technology transfer, provided there will be sufficient incentives and support for investment in technology renewal by enterprises. With respect to their export strategy Vietnamese enterprises are advised to strengthen their efforts to gain the advantages of registering their own trademarks, brand names etc. and build up customer confidence on export markets.

**Export promotion will have to be done** without direct subsidies. The essence of the multilateral rules-based system for international trade is to provide every country and every enterprise with a level playing field for competition by preventing unfair trade practices like export subsidies, and also price dumping on export markets by individual enterprises. Having become a WTO member, Vietnam will have to phase out direct export subsidies. This is an economically sound policy because financial subsidies cannot lead to sustained export success if the products are not competitive. The debate is still ongoing as to whether indirect export subsidies like tax exemptions for enterprises in Export Processing Zones or Duty



Drawback Schemes belong to the measures banned. In any case, Vietnam would be well advised to concentrate on its genuine competitive advantages in labour intensive and, at the same time, high quality goods and refrain from creating artificial competitive advantages through export subsidies. It should not be forgotten that export subsidies are a transfer of economic resources from the exporting to the importing country. The importing country could either impose a countervailing duty, which would skim off the subsidy margin and contribute to the state budget, or the consumers could be given the opportunity to buy the subsidised import goods at a lower price. Of course, it would not make sense if Vietnam would transfer resources to the importing countries through subsidising its exports. Even then, the government can do a lot to promote competitiveness of Vietnamese enterprises on export markets by means compatible with WTO rules. In order to increase competitiveness, it is necessary to remove existing obstacles for (potential) exporters and to level the playing field between state-owned and private enterprises. The investment climate for foreign investors should be further improved to attract more export-oriented Foreign Direct Investment (FDI). In addition, export promotion activities can support domestic companies in their effort to become successful exporters. These activities include the provision of information on export markets and better presentation of Vietnamese products in the developed countries, where not many buyers and importers know how developed and diversified the capacity of Vietnam already is for supplying not only a range of commodities, but also high quality handicrafts and manufactured goods (garment, household goods, furniture etc.).

**A precondition for successful exporting is to adjust Vietnamese export products to standards and norms of export markets.** With the dramatic decline of tariffs in most countries as a result of past GATT Rounds – and the present and future WTO Rounds will bring down tariffs further –, other trade barriers have become more and more important. The host of new technical norms, health, environmental and social standards mainly in Europe, but to a lesser degree also in the other industrialised countries, can become effective trade barriers. Vietnamese firms having produced mainly for the domestic market in the past, still have little awareness of the standards, norms and quality requirements on export markets. Above all, there is a lack of knowledge of and direct experience with the importance of *product* standards. Many Vietnamese enterprises still focus on *production process* standards like International Standards Organization (ISO) stan-

dards. In order to correct this bias, government agencies and business associations should provide more information and more assistance to exporting enterprises for making their products comply with safety, health and environmental standards of export markets. In addition to that, the institutional infrastructure for testing and certification of export products has to be improved in Vietnam. Exporting firms need certificates from accredited agencies and testing laboratories to prove to overseas buyers and consumers that their products comply with the standards required by the EU and other developed countries. One should not be mistaken: The issue of standards and norms of export markets is relevant regardless of WTO accession. Compliance with these standards in general is a necessary precondition for exporting products. The importing country has the right to apply its national standards to imported products, as long as the standards can be justified by the need to protect public security or the health of consumers and are not used in a way to discriminate against imported goods. Exporting countries have to comply with the standards of importing countries regardless of WTO membership. Vietnamese exporters of aquaculture products have already gained experience with tighter standards introduced by the EU to protect consumers' health. In case of conflict, the WTO Agreements on Technical Barriers to Trade (TBT) and on Sanitary and Phytosanitary Measures (SPS) provide some guarantee against misuse of standards and norms for protectionist purposes, but it will be extremely difficult to find evidence for abuse since these standards are routinely applied to the same domestic products.

Successful East Asian industrializing countries have followed protectionist trade policies and dirigiste industrial policies at an earlier stage of their economic development. Today, WTO rules no longer allow implementing the core policies and instruments of the East Asian model, like infant-industry protection, export subsidies or reverse engineering. However, in a globalizing world, such policies may no longer be appropriate in view of some of the new features of globalizing industries. Therefore, Vietnam should not focus too much on how to copy the example of earlier industrialising countries in the region. With such a strategy, Vietnam would only trail behind the other countries, which are also moving forward.

To conclude, as a WTO member, Vietnam will have to change some of the instruments of its industrial policy. This has the following implications on the different levels: On the macro level, providing a level playing field for private, state-owned and foreign invested enterprises will probably be the

most important task. On the meso level, institutions like business associations and chambers of commerce have to gain influence on the macro level and publicity on the micro level. On the micro level, enterprises must increase competitiveness and inform themselves more intensive about the characteristics and requirements of export markets. Vietnam can expect effective support from the donors for its adjustment programmes and for the training of government officials and the business community in all aspects of WTO rules and agreements. The international debate on *aid for trade* has come to the conclusion that trade liberalisation is a necessary, but not sufficient condition for export expansion and diversification of developing countries. Whatever the outcome of the Doha Round will be, trade-related development assistance will have to play an important role to make a country like Vietnam capable of administering the various new WTO agreements and help its exporters to make use of the new trading opportunities that should be the result of a successful *Development Round*.

## 1 Background and research design of the study

In 1995, Vietnam submitted the application for accession to the World Trade Organization (WTO) and is now preparing to become the 150th WTO member state. Joining the WTO will be another important step in Vietnam's economic integration into the global economy. Yet, in order to reap the fruits of international economic integration, Vietnam will have to improve the competitiveness of existing and new industries so that they will be able to withstand increasing competition at home resulting from import liberalisation and succeed on export markets. East Asian countries have shown how an active industrial policy stimulating and directing the industrialisation process can be combined with an export promotion policy that encourages the new industries to find their way to the world markets. Vietnam should be able to follow their example and become another *Asian (transition) tiger* (Van Arkadie / Mallon 2003). But will that be facilitated or hindered by WTO membership?

Since the beginning of the 1990s, there is a heated debate about the reasons for the *East Asian Miracle*. The conventional view, favoured by the Washington-based international financial institutions World Bank and International Monetary Fund (IMF), sees the success of the East Asian Miracle countries as a result of sound macroeconomic policies based on extraordinarily high savings rates, combined with heavy investment into infrastructure and education and an open-door policy towards foreign investment. This interpretation of the East Asian Miracle has been challenged by a number of heterodox economists and political scientists who stress that developing countries in Africa and Latin America which applied the structural adjustment programmes prescribed by the World Bank and the IMF have not achieved the same growth rates as the East Asian countries with their specific policy mix of sound macroeconomic policies *and* active industrial policies plus export promotion to make the new industries gain experience on the world markets and become competitive with the industries of the developed world. The debate between mainstream economists and their heterodox critics on the best policy for industrial development of less developed countries remains inconclusive, both sides find empirical proofs in one or the other country for their viewpoint. Only one new aspect would be accepted by almost all development economists, and that is the decisive role of *institutions* in developing countries that are

either able or not to design and implement the set of economic and industrial policies most appropriate for their country.

Soon after the WTO had succeeded the GATT in 1995, it became the central target for the anti-globalisation campaign. During the Uruguay Round the GATT, Contracting Parties had negotiated several new agreements that widened the mandate for the WTO, covering not only border measures like tariffs and quotas (that had been the area of the GATT), but also an increasing range of other trade-related policies – and more will come, since in the age of globalization it is difficult to think of an economic policy that has no impact on international trade and competition for foreign investment. The new agreements had been signed by all WTO member countries (*single undertaking*), i. e. developing countries had committed, for the first time, to make their trade-related policies comply with the multilateral rules and agreements of the WTO. The obligation to full compliance with all WTO agreements is relaxed only by the *special and differential treatment* provisions based on Part IV of GATT and built into all WTO agreements. But in view of increasing competition from the rapidly industrializing countries, there is mounting pressure from developed countries that special and differential treatment should be confined to the least developed countries, whereas the more advanced developing countries should graduate from their special status and comply fully with all rules and agreements of the WTO.

Whatever different motives and interests have brought the protesters against WTO ministerial conferences together – trade unions of industrialized countries and environmentalists complaining about unfair competition from developing countries that do not apply the higher social and environmental standards as the developed countries, Third World activists and Non-governmental Organizations (NGOs) complaining about the asymmetry of the world trading system and the unfair treatment of developing countries in the multilateral rounds of trade negotiations – through the anti-WTO campaigns governments of developing countries became aware of the potential repercussions of the extended and tightened rules and agreements they had signed collectively at the end of the Uruguay Round. Thus, they blocked the launch of a new round of trade negotiations at the 1999 WTO Ministerial Conference in Seattle, and accepted new negotiations at the 2001 Ministerial Conference in Doha only after the EU and the US had promised to take the concerns of developing countries about the

unbalanced outcome of the Uruguay Round seriously. The label Doha Development Round recognized this promise. However, neither the EU nor the US have met their promise yet, so the Doha Round has been suspended mid 2006, revealing the deep disagreement between developed and developing WTO members on what would make the round a true *Development Round*.

The present study has been motivated by the new wave of criticism of the WTO and its impact on developing countries' prospects for promoting industrial development and export diversification through active policies. The criticism has to be taken seriously, especially since a number of eminent economists have contributed to it, blaming not so much the WTO, but the major players US and EU, for their neglect of developing countries' interests to actively promote industrial development. According to the critics, the new agreements negotiated in the Uruguay Round restrict the capacity of late industrialising countries like Vietnam to implement the same active industrial policies that the more advanced East Asian industrialising countries had pursued at an earlier stage of their development.

The debate will be followed closely by the countries preparing for accession to the WTO. When the Vietnamese government and the Communist Party took the decision to apply for WTO membership in 1995, they may not have been fully aware of the implications of the widened WTO mandate for Vietnam's economic and industrial policy space. Even incumbent developing countries realised only some time after the end of the Uruguay Round what unfavourable deal they had accepted and what costs the implementation of the new agreements (especially the TRIPS Agreement) would entail.<sup>1</sup> Taking the critical arguments into account, should the Vietnamese government reconsider WTO accession and rely instead on bilateral and regional trade agreements with its main trading partners? Or will a closer scrutiny of the implications of the most relevant WTO rules and agreements reveal that the costs of implementing them are worth while to bear as part of the general programme of market economy reforms which

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1 With the *single undertaking* of the Uruguay Round (with only four exceptions, all WTO members subscribed all agreements negotiated during the round) developing countries had accepted a number of new obligations with a real price tag, whereas the developed countries had only promised to phase out in the medium term future protectionism against products of special interest for developing countries, i. e. agricultural goods, textiles and clothing, a promise which has not been kept until today in the case of agricultural trade.

Vietnam is pursuing since 1986? In that case, the costs of making Vietnam's trade and industrial policies consistent with the WTO framework would be acceptable with respect to the benefits of secured access to export markets, and access to the effective WTO Dispute Settlement Procedure in case of conflict with a trading partner.

What can Vietnam's economic policy makers learn from that debate, and what type of industrial policy and export promotion should they pursue in the future that does not conflict with the WTO rules and agreements and makes Vietnam's industries fit for their integration into the global production networks that have become a dominating feature of the present stage of global economic integration? In order to find answers, the study will first present the general implications of the new WTO agreements for industrial policies of member countries and discuss their economic rationale from the different positions in the debate on industrial policy and the East Asian Miracle. After this introduction to the new WTO framework for industrial policies and export promotion, the most relevant implications for Vietnam's industrial policies and export promotion will be reviewed in detail and conclusions drawn on how the remaining policy space for improving the competitiveness of Vietnam's industries should be used. After having joined the WTO, Vietnam will have to develop industrial policies and export promotion measures that are consistent with its own economic conditions and in conformity with WTO rules and agreements.

The present study explicitly focuses on the challenges of WTO accession for industrial policy and export promotion – thus leaving aside other WTO issues, like agricultural trade and trade in services. This focus is based on the assumption that industrial development – and export diversification and promotion as part of it – is the most important prerequisite for Vietnam's successful integration into the global economy. The experience of developing countries in general – and of East Asian newly industrialising countries (NICs) in particular – shows that a diversification of the export structure including industrial goods is needed for sustained economic growth and exports.

The study does not attempt to assess the costs and benefits of WTO membership. The Vietnamese government will have done a rough cost-benefit calculation of WTO membership with the costs of adjusting legislation and trade-related policies to the WTO rules and agreements and the benefits of secured access to global export markets for Vietnam's widening range of

agricultural and manufactured exports plus increasing attractiveness for foreign investors. However, three main benefits and opportunities for Vietnam can be mentioned here already: First, WTO accession will strengthen domestic policies and institutions by modifying existing laws and introducing new ones that are intended to liberalize markets and to strengthen the private sector. Second, WTO membership will improve and secure the access to major export markets – at least in the long run, because the US and the EU will treat Vietnam for the next decade as a non-market economy which will facilitate launching anti-dumping measures against Vietnamese exports. Third, as a WTO member Vietnam will have access to the new dispute settlement mechanism for trade policy conflicts.

In contrast, challenges and problems of Vietnam's WTO accession are strongly related to the institutional framework. On the one hand, the co-ordination of the negotiation concerns different ministries and lacks coherence, communication and co-ordination. On the other hand, the coordination of policy reform seems to be weak and faces three problems in particular: a low level of awareness of the implications of WTO membership, opposition of potential losers and vested interests. Apart from institutional problems, there are economic challenges arising from WTO accession. For example, adequate adjustment policies to balance disruptive effects of trade liberalisation need to be developed.

The present study starts from the Vietnamese government's decision to become WTO member and asks what implications WTO membership will have for the country's industrial policy and export promotion.

### *Research design and empirical base*

The core chapters of the study dealing with the main implications of WTO membership for Vietnam's industrial policies and export promotion are based on interviews with government officials, representatives of specialized agencies and business associations, with a sample of enterprises in and around Hanoi and Ho Chi Minh City, and with donor agencies involved in WTO-related activities were carried out during the field visit of the team in 2004. The chapters on the new framework of the WTO for industrial policies and the debate on industrial policy, and on Vietnam's reform process, as well as new information to the core chapters that came up in the meantime, have been added thereafter.



The interviews in Vietnam were conducted on three levels:

- The **macro level**, representing the level of policy making. A major question asked by the study team on this level has been: Which reforms will the Vietnamese government and the different ministries have to implement in order to bring industrial policy and export promotion into conformity with the various WTO Agreements?
- The **meso level**, representing the level of intermediate institutions between the government (macro level) and the business sector (micro level) like, e. g., business associations. Influencing government policy making from below has taken place in Vietnam so far mainly through personal contacts and informal channels. However, meso level institutions will become more important as interest representing and information channelling institutions. The questions asked focused on the perception of meso institutions regarding the preparations of Vietnam to meet WTO requirements and the changes to be made regarding Vietnam's industrial policy and export promotion aiming at integrating the country into the global economy.
- The **micro level**, representing industrial enterprises. There are three different legal forms of industrial enterprises in Vietnam: state-owned enterprises (SOEs), foreign invested enterprises (FIEs), and Vietnamese private owned, mainly small and medium enterprises (SMEs). Of course, each type of enterprise and the different industries will be affected differently by the necessary changes of Vietnam's trade and economic policies with respect to compliance with WTO rules and agreements. Therefore, the main questions of the study team focused on the perception of managers and entrepreneurs in industry of the challenges of the WTO accession as well as on their awareness and preparations regarding Vietnam's economic integration into the global economy in general.

The main instruments for data generation have been semi-structured interviews with institutions on the macro and the meso level and with different kinds of enterprises. On the macro level, interviews were carried out with relevant ministries and subordinated administrative institutions. On the meso level, business associations and chambers of commerce have been interviewed. On the micro level, different legal forms of enterprises (SOEs, SMEs, FIEs) in different industries have been interviewed. There was no explicit sectoral focus, but interviews were mainly carried out with enterprises in the following industrial branches: garments, textiles, footwear, automobiles, motorbikes, electronics, processed food and furniture.

In total, 90 interviews and informal talks have been carried out by the study team (see Appendix: Table 10). Furthermore, relevant government documents, research papers and other material related to the issues of the report were taken into consideration.

### *Road Map of the report*

Chapter 2 gives an introduction, especially for readers not familiar with Vietnam, to the country's transition from a centrally planned socialist economy to a mixed economy integrating into the regional and world economy. It gives an overview over the political setting and an introduction to Vietnam's global economic integration process from *doi moi* to WTO accession.

Chapter 3 gives an introduction to the debate on industrial *policy space* under the new WTO rules and agreements. It is difficult to see today where the rising tide of criticism of the alleged unfairness of the system will lead to, but since the asymmetry between rich and poor, large and small trading nations will not change in the foreseeable future, and economic power will translate into negotiating power in all international organizations, developing countries should not expect to gain much from the debate on the narrowing policy space, at least not in the short run. They should utilize the remaining policy space and promote their industries with measures that are not in conflict with WTO agreements.

In chapter 4, the changing framework for Vietnam's industrial policy under WTO rules will be examined. What are the restrictions and remaining options for industrial policy under WTO rules? Each of the three topics studied in this chapter – import liberalisation, localisation policy and enforcement of IPRs – is examined in the following way. Firstly, the respective WTO Agreement will be sketched briefly: Regarding import liberalisation, corresponding parts of the GATT will be presented; regarding localisation policy, the Agreement on Trade-Related Investment Measures (TRIMs) will be studied and in the chapter concerning IPRs the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) will be dealt with. Secondly, challenges for Vietnam's industrial policy regarding each of the topics will be discussed.

In chapter 5, challenges for export promotion will be discussed. Firstly, the WTO Agreement on Subsidies and Countervailing Measures will be ex-

amined in a similar manner like the WTO topics in chapter 3. Against this background, WTO compatible export promotion instruments will be discussed. Since compliance with technical, health and environmental standards and norms on export markets becomes an increasingly important challenge for exports of developing countries, these issues will be dealt with in detail.

In chapter 6, conclusions will be drawn on industrial policy and export promotion in Vietnam. An overview of donor activities in the area of aid for trade is given with the recommendation to use training programmes not only for the necessary know-how transfer on many technical issues of the multilateral system of the WTO, but also to stimulate the debate in Vietnam between the government, the business community, the civil society and the academic community on trade and trade-related policies and how Vietnam will have to use the remaining policy space for making the three segments of its industry, i. e. state owned enterprises, foreign invested companies and private business, cooperating more effectively so that Vietnam will be able to diversify its exports and have a rising local content in manufactured exports. At the end, an overview is given on the donor activities related to WTO accession and implementation of the new obligations.

## **2 Vietnam's transition to an open market economy**

### **2.1 The political framework: A constitutional, law-governed single party state**

According to the 1992 Constitution (amended in 2001), Vietnam is a *Socialist Republic* with the Communist Party Vietnam (CPV) as the *leading force* of the state and society. Although the Communist Party shows no intention to give up its leading role enshrined in Article 4 of the Constitution, it has allowed and even propagated a remarkable process of governance reforms which aim at combining the goal of economic growth and development through market economy mechanisms with the goal of social stability and participation of the various social groups and regions in the process of political decision making and legislation. According to an official source "*Vietnam is a law-governed socialist state under the leadership of the Communist Party.*" (Vietnam Trade Office in the United States of

America, Website, “Political System”). The commitment of Vietnam’s Communist Party to a constitutional system and to the rule of law has deep roots in Ho Chi Minh’s Declaration of Independence (1945) which fore-saw democratic elections and the adoption of a Constitution by the People’s Parliament that was legitimated by general elections in January 1946.

The Communist Party of Vietnam has a well-defined internal decision-making process. A Party Congress meets once every five years. The 10th Party Congress of the CPV met in April 2006 in Hanoi. A total of 1,176 delegates representing 3 million party members attended the opening ceremony. The Congress elected a new Central Committee with 160 members and a Politburo of 14 members. The Central Committee meets at least twice annually, usually to confirm the policy which is designed by the Politburo. As the Party’s supreme decision-making body with unlimited policy-making powers, the Politburo sets the direction of the party and the government. Senior Politburo members hold high position in the government and the National Assembly, the Vietnamese version of a parliament. As all important government posts are filled by party leaders and party cadres, the government is mainly implementing party policies. The CPV dominates state institutions and mass organizations, such as the Confederation of Trade Unions, the Women’s and the Youth Union. The Party exercises its control within a decision-making paradigm that may be termed “consensus governance” which means a slow and careful decision-making process involving and assigning responsibilities to many stakeholders. This has made Vietnam’s fundamental economic and societal changes possible, without challenging the leading role of the Party.

An important element in this consensus governance is the National Assembly in which legislation and government policies are debated. The National Assembly meets twice a year for 7–10 weeks each time. Its 500 deputies are elected every five years. The deputies of the National Assembly should represent all social groups and regions of Vietnam, including non-Party members. Besides its legislative function, the National Assembly elects the president of the state and the prime minister, and approves the members of the government cabinet, nominated by the prime minister. Despite the central political role that the Constitution attributes to the Communist Party, the National Assembly plays an increasing role as the highest representative body and only institution with legislative powers. *“All state bodies are held accountable to, and are appointed by, the Na-*

*tional Assembly. Over time, the National Assembly has enhanced its legislative role and oversight of executive government bodies, and the CPV is committed to further enhancement of the National Assembly's role.”* (ADB 2001, 54) Of course, with about 80 % of the deputies being party members, the National Assembly is not independent of the Communist Party. But there are increasingly open debates about the new economic legislation required for market economy reforms and international economic integration, and about other issues of government policies and even behaviour of government officials and party members, e. g. corruption cases. *“As a reflection of the increasingly open dialogue between the state and society, the investment law draft was strongly debated in the National Assembly and the media, with many deputies and business groups openly criticizing it for exacerbating bureaucratic red tape for domestic investors.”* (Luong 2006, 152)

Despite the leading role of the Communist Party, Vietnam is not a monolithic state in which the political centre can implement economic reforms top down without opposition and resistance from those groups and organizations that fear to lose from economic liberalisation. And, what seems to be natural for a Communist Party, there is ideological opposition from within against the entire market economy reform programme. *“The conservative members of the leadership in Vietnam are strong believers in socialist orthodoxy. After a lifetime of belief in Marxism, they are uneasy about the market economy. (...) The conservatives want funds and technology from outside but fear that ideas such as democracy, human rights, civil society, governance, and so on, will infiltrate the country and undermine Communist Party dominance. They perceive the market economy, albeit with a socialist orientation, as a corrosive force and that reforms have outpaced the capacity of the CPV to guide it.”* (Dinh 2000, 365) The reformers on the other hand, argue for further economic and administrative reforms as a precondition for Vietnam to catch up with its more advanced neighbours, which have successfully implemented market economy reforms and integrated their economies into the globalizing economy. The political weight of the reformist faction is strengthened by Vietnam's accession to ASEAN, the signing of the bilateral trade agreement with the United States and by the application for WTO membership. The process of gradual international economic integration makes past economic reforms irreversible and requires further legal and institutional reforms towards a market economy.

## 2.2 The legal framework

The weakest element of Vietnam's governance seems to be the legal system. Since the beginning of the economic reform process in 1986, the legal system of Vietnam has developed rapidly, however unevenly, with its main focus on legislation, whereas the other elements of a functioning legal system – legal institutions, legal education and training, legal information – have lagged behind. After more than a decade of legal reforms necessary to implement economic reforms and to establish a functioning market economy, the Vietnamese legal system is still a mixture of imported commercial legislation and local traditional principles and practices. *“Despite the enactment of commercial legal framework largely based on western legal transplants (laws and legal practices), Vietnam’s legal system overwhelmingly resonates with local rather than imported principles, precepts and processes.”* (AusAID 2000, 1) *“The quality of laws and regulations is weak in several respects. Superior and subordinate regulations are often inconsistent. Sometimes provisions contradict each other. The resulting uncertainty is aggravated by the practice of not precisely specifying what provisions of previously issued legal documents are to be abrogated when a new legal document takes effect. The mechanism for reviewing draft legal documents to check their constitutionality, legality, uniformity, consistency, and enforcement feasibility is also still weak.”* (ADB 2001, 58) Finally, the enforcement capacity is weak. There are not enough lawyers and judges to implement economic legislation and to settle commercial disputes between economic agents. *“Many judges do not have legal training and their appointments are based on patronages. The credibility of the system is low, and viewed as open to bribery.”* (ADB 2001, 60) An increasing backlog of unsettled civil lawsuits reveals the shortcomings of the legal system.

As a special feature of a law-based state and a market economy in which private enterprises operate independently of government economic management but are subject to government regulations and licenses, there is a need for administrative jurisdiction. Thus, in the early 1990s, Vietnamese delegations studied the experiences with administrative courts and jurisdictions in Western and Asian countries. As a first step, since 1996, administrative divisions were established within the people's courts at the central and provincial levels (Quang Nguyen 2004). Of course, it takes time before such a new system will be fully operational and effective. As

long as legislation itself is inconsistent and even contradictory, administrative courts cannot fulfil their function to make government organizations more accountable to the people in case of conflict, and a wide discretion remains for the bureaucracy. This leads to uncertainties as to whether one can rely on a decree or a law, even if it has passed the National Assembly.

The Government – and even a representative of the Communist Party<sup>2</sup> – has recognized the shortcomings of the legal system and formulated a “*Comprehensive Needs Assessment For the Development of Vietnam’s Legal System to the year 2010*” (Inter-Agency Steering Committee for Vietnam’s Legal System Development Assessment 2002). The report provides a balanced picture of the state of Vietnam’s legal system. On the one hand, it presents the achievements since the beginning of the reform policy in 1986: “*In the last 15 years, the number of laws and ordinances promulgated were double the number of such legal documents promulgated during the preceding forty years (1945–1985). With such new laws and ordinances we have created a legal framework that facilitates the development of a socialist oriented market economy which will gradually replace the old centrally planned economy, and creates a legal basis for comprehensive reform of the country.*” (Ibid., 9–10) The report points to the increasing number of international treaties signed by Vietnam, which have “*gradually become an integral part of the Vietnamese legal system.*” (Ibid., 10) On the other hand, the report of the Inter-Agency Steering Committee analyses in detail the shortcomings of Vietnam’s legal system, such as the imprecision and frequent changes of laws and regulations that leave too much room for interpretation by implementing agencies and the possibility that implementing guidelines contradict the objectives of the legislation. The report acknowledges that the capacity of judges is not adequate, a problem that is related to both imprecise and sometimes contradictory legislation and regulation, and to the insufficient quality of legal education and training.

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2 “*Vietnam’s legal system generally remains weak and inadequate, failing to catch up with, and meet the requirements of, the process of national industrialization and modernization and building a law-governed State of the people, for the people and by the people.*” (Nguyen Van Yeu, Member of the Party Central Committee, Vice Chairman of the National Assembly: Orientations for Perfection of the Legal System in the Coming Time, in: Vietnam Law & Legal Forum, 13.01.2005; online: [http://news.vnanet.vn/vietnam-law/Service.asp?CATEGORY\\_ID=5&SUBCATEGORY\\_ID=10&NEWS\\_ID=456](http://news.vnanet.vn/vietnam-law/Service.asp?CATEGORY_ID=5&SUBCATEGORY_ID=10&NEWS_ID=456))

In view of the long interruption of a smooth development of the legal system during the 30 years of war for national liberation, and in view of the simultaneous changes that have taken place since the beginning of the reforms – *“from an outmoded agricultural economy into an industrial economy; from the closed and barter economy into an open economy with international integration; from the centrally planned economy into a market economy with a socialist orientation; and from a state managed by administrative commands into a rule of law socialist state”* (Inter-Agency Steering Committee 2002, 18) – it is obvious that the legal system needs time – perhaps decades and not years – and technical assistance to become fully effective as a reliable framework for all actors in the market economy. On the basis of the comprehensive needs assessment presented by the Inter-Agency Committee, Vietnam can rely on the willingness of the international community to provide whatever donor assistance is necessary for the development of the country’s legal system. This is especially true in view of the additional requirements for legislation and institutional development for implementation related to the preparation for WTO accession. One can only hope that Vietnam’s implementing agencies and the judges and lawyers will be able to absorb and manage the huge amount of new economic legislation that Vietnam has to carry out and implement on the way to an open internationally integrated socialist market economy.

### 2.3 The process of economic transformation

The communist-led government of Vietnam has shown a remarkable flexibility in responding to economic challenges. After the war and the unification of North and South Vietnam in 1975, there was a ten-year phase of experimentation with Soviet-style central economic planning, nationalization of all economic activities and concentration of investment on state-owned industries. This strategy was not successful, especially the collectivization of agricultural production which met with strong resistance from the farmers. There was a serious recession between 1976 and 1980, with both agricultural and industrial production declining, high inflation and sluggish growth during the 1980s. Due to low agricultural productivity, Vietnam had to import large quantities of food and became dependent on foreign aid, mainly from the Soviet Union. Exports were insignificant, and foreign trade was monopolized by the government. During the 1980s, it became obvious that the strategy had failed and that there was no alterna-



tive to economic reforms. Vietnamese economic policy makers could refer to the example of China where the market economy reforms since 1978 had triggered off a real “great leap forward”. With the breakdown of the Soviet economic block in 1989/90, Vietnam could no longer rely on foreign aid from the Soviet Union and had to approach Western donors and international aid agencies for technical and financial assistance.

Early economic reforms in Vietnam started in 1982, when the Fifth National Party Congress “*sanctioned privately owned small enterprises and the ‘family economy’ for agriculture.*” (ADB 2001, 53) Vietnam’s farmers and household enterprises made use of their new economic freedom, and the increase of agricultural production opened the door towards deeper economic reforms. In 1986, the full economic transformation from a command economy to a “socialist-based market economy” was endorsed by the Sixth National Congress of the Communist Party under the slogan of “*doi moi*” (*economic renovation*). The transformation began in the agricultural sector by redistributing land to rural households and by leaving production and marketing decisions to the farmers who responded to the incentives of market prices.

The early *doi moi* reforms had four fundamental components: 1. dismantling of central economic planning in favour of letting market forces determine prices, 2. encouraging private business development responding to price incentives, 3. macroeconomic stabilization, 4. opening the economy to international trade and foreign investment and promoting Vietnam’s integration into the regional and global economy. In contrast to the *big bang* style market reforms of some Eastern European countries, Vietnam’s economic reformers pursued a gradualist strategy of introducing market economy mechanisms without abandoning government control and management of the state-owned enterprise sector. Thus, the planned economy was replaced by a “multisectoral economy” (*mixed economy* in the terminology of Western economics) in which different forms of ownership – state-ownership, cooperative and private ownership and foreign investment co-exist. The market is the principle coordinating mechanism, but the government still claims a strong steering function. Despite the explicit recognition of the private sector, the government still prefers the promotion of the state sector and restrains the private sector.

Gradual trade liberalization was an essential element of Vietnam’s economic reform programme. Since 1989, the state monopoly in foreign trade

was dismantled step by step. The first step was to allow individual companies to enter into trading activities, however under relatively restrictive conditions. These could be met only by state owned enterprises. Restrictive trade licensing was relaxed in 1998 and abandoned in 2001. *“From then on all domestic enterprises have been allowed to trade commodities or items freely, except those prohibited or under specialized management. (...) Since 2002, the foreign enterprises have also been granted the right to export goods other than those they produce.”* (Vo Tri Thanh 2005, 77) Non-tariff barriers, especially quantitative restrictions, which had been used to balance supply and demand of the economy, to protect domestic production and to prevent foreign exchange crises were removed in 2001, except for a few sensitive products, like petroleum and sugar. Quantitative restrictions deemed necessary to protect certain agricultural products were replaced with tariff-rate quotas. The old system of monopoly state trading could do without import tariffs; they were first introduced in 1988. The tariff system was frequently expanded and adjusted according to the protectionist interests of individual industries and agricultural producers. When the quantitative restrictions were abandoned in 2001, tariff rates were increased to some extent in order to provide a similar degree of protection for the same products. Tariffs will have to be reduced again with the commitments to trade liberalization that Vietnam has accepted under various regional trade agreements and in view of WTO accession.

The early doi moi reforms triggered off a rapid expansion of output, foreign trade and employment, which made Vietnam one of the fastest growing economies in the region at least until the Asian crisis in 1997/98 caused a slowdown showing Vietnam’s increasing economic integration in the region.

Until today, one of the most difficult and contested aspects of Vietnam’s economic reforms is the adjustment of the state-owned enterprise sector to the conditions of a market economy. The SOE sector was established in the 1950s and 1960s as part of the Soviet development model aiming at rapid industrialization of underdeveloped countries through nationalization of existing industries and massive government investment in newly established public sector industries. *“As a result of this development strategy, by the end of 1960, 100 per cent of industrial establishments, 99.4 per cent of commercial establishments, and 99 per cent of transportation facilities,*

*which once belonged to foreign and Vietnamese capitalists, were nationalised and transformed into SOEs.” (Ngu 2002, 2–3)*

The reforms of the state enterprise sector started in the mid-1980s as part of the general economic renovation programme. SOEs were given more autonomy, and the budgetary support was made less automatic in order to enforce a higher degree of efficiency. During the 1990s, the next round of reforms aimed at consolidating the state enterprise sector by reducing the number of SOEs (from 12,297 in 1991 to 6,264 in 1994) through liquidation, equitization and mergers. Nevertheless, the management remained dependent on superior authorities, like the central, provincial or municipal governments, ministries or the military, which act as owners of SOEs. Since then, the process of SOE reforms has slowed down due to a number of obstacles.<sup>3</sup> Several interested groups resist equitization: Line ministries and people’s committees will lose the benefits from controlling and operating SOEs, the managers, often appointed by the Party, will lose their privileges, and the workers in SOEs may face the risk of losing their jobs. Managers of large SOEs have invited foreign investors for modernizing production and gaining access to export markets, thus defending the existence of their SOEs against full privatization. These anti-reform interests find ideological support from the conservative faction in the CPV that questions the rationale of giving away public assets and an important instrument of industrial policy for the sake of market economy principles. According to the ‘conservatives’, the government should keep majority shares in large SOEs, which are seen as strategic instruments for industrial development and for achieving certain social goals like employment or development of backward regions. As a consequence of WTO accession however, the pressure for continuing reform of the state enterprise sector will increase.

SOE always kept and many still keep a dominant role in highly protected key industries counting for a large share in output and export volume. Due

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3 “In general, the SOE reform process remained slow and failed to achieve the objective of basically completing the SOEs restructure and reform by 2005 as planned. (...) The equitized state assets remain low despite significant increases in the share from about 6-7 % in 2004 to about 12 % in 2005. Equitization is mainly being implemented in small-scale enterprises (...); few enterprises with state capital of more VND 20 billion are being equitized although there is almost no legal limit in place on that.” (CIEM 2006, 64, 66-67)

to protection and preferential treatment from the government in every respect, the state sector will face difficulties with adjusting to higher competition levels through international integration. In contrast to the private sector, SOEs never faced severe rivalry of competitors in their respective industry, and they had always access to unlimited financial resources. Thus, most of the Vietnamese SOEs have low performance indicators, lack competitiveness, suffer chronic losses, are overstaffed and have outdated technologies. However, some SOEs performed very well during and after their equitization and are gaining competitiveness.

The Enterprise Law and the new Law on Foreign Investment have already improved the legal framework for a market economy. However, only slow progress has been made in the equitization of SOEs. In 2003, out of total 4722 SOEs, 537 enterprises were equitized and another 408 enterprises rearranged (merged, unified, went bankrupt etc.) which accounts for only 62 % of the original plan. Until 2005, the government plans to keep 1931 enterprises with 100 % state capital. 2053 SOE will be equitized and 738 rearranged. In almost half of the equitized SOEs the government will hold the majority of the shares.

In 2003, SOEs still contributed 38 % of Vietnam's Gross Domestic Product (GDP) and 50 % of the export value. This is particularly striking on the one hand because SOEs bind a lot of Vietnam's financial resources owing almost 80 % of total domestic credits. On the other hand, an estimated 20 % of underemployment and redundant labour in SOEs are a big challenge for improving the efficiency of SOEs. Although SOEs employ only 10 % of the total work force, reducing the inefficiency of SOEs will not be possible without some layoffs.

Despite the declared goal of progressive equitization (the Vietnamese reformers avoid the word *privatization*) of SOEs, up to date only smaller and less profitable SOEs have been equitized, In contrast to the policy towards SOEs, the policy towards private enterprises tends to be restrictive. There are many restrictions on private enterprises like the licensing obligation and many administrative checks, which curtail the growth of the private sector and thus the creation of jobs. Besides, compared to SOEs, private enterprises still suffer discrimination concerning access to credit, land and foreign trade licenses.

Concerning the financial sector, there was a cautious and gradualist approach to reforms: step-by-step liberalisation, a gradual transformation of existing financial institutions and the creation of new ones. The general focus has been on stability. This approach has proved successful on the whole and macroeconomic destabilisation has been avoided. Nevertheless, Vietnam is still far from having a modern market-economy financial system. The credit supply to the business community, especially to small- and medium-sized enterprises is still insufficient. This is mainly due to the fact that commercial banks suffer from the burden of non-performing loans to the state-owned enterprises. The development of private enterprises is severely constrained by their difficult access to loans from the banks. They have to generate their investment funds from their own profits or have to borrow from relatives and friends, which leaves little room for major investments.

Foreign direct investment contributes increasingly to economic growth, employment, exports and technology transfer. In the first years since the lowering of external barriers, investment was concentrated in the oil industry and in real estate sectors. Nowadays export-oriented manufacturing of consumer goods in the clothing, footwear and food-processing industries and inward-oriented investment in domestic electronics and vehicle manufacture are gaining importance. However, Vietnam's investment climate for foreign investors is regarded to be less favourable than that of other industrializing countries in Southeast Asia. There are many problems concerning the relationship between foreign enterprises and Vietnamese authorities, caused by arbitrary and often unpredictable interference by the authorities.

## 2.4 Vietnam's integration into the regional and global economy<sup>4</sup>

Vietnam is strongly committed to open up its economy and to integrate into the global economy. However, its reintegration into the world economy takes place at a time when international trade policy is becoming increasingly complex. Besides the multilateral trading system of the

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4 In this chapter only the most important integration projects are referred to, excluding for example the Asia-Europe-Meetings, that take place every two years since 1996.

GATT / WTO, a complex web of sometimes overlapping regional free trade agreements (FTAs) and bilateral trade and economic partnership agreements is building up (cf. Bonapace 2005, Banda / Whalley 2005). The recent surge of new trade agreements among Asian countries and between Asian and overseas countries can be taken as an indicator of the weakening faith in the multilateral system, especially after the failed WTO ministerial conferences of Seattle 1999, Cancun 2003, and the present (fall 2006) suspension of the Doha Development Round. But the increasing complexity of the web of bilateral, regional, interregional and multilateral trade agreements and the strain for the negotiating capacities, especially of late-coming countries like Vietnam, could become an incentive to concentrate again on negotiating for a successful conclusion of the Doha Round of multilateral trade negotiations. Yet, the old debate among economists and trade policy makers whether regional and bilateral trade agreements are *stepping-stones* or *stumbling-blocks* to the multilateral trading system remains inconclusive. For the foreseeable future, there will be no change of the multi-layer trading system, and Vietnam will have to negotiate in parallel on all three levels, the multilateral, the regional and the bilateral level.

#### *ASEAN Free Trade Area (AFTA)*

On 28 July 1995, Vietnam became a full member of the Association of Southeast Asian Nations (ASEAN) and committed itself to implement the necessary requirements resulting from the different ASEAN integration projects. At the 4th ASEAN Summit in Singapore 1992, the ASEAN heads of government had agreed to establish an ASEAN Free Trade Area (AFTA) within a 15-year period; this was later reduced to a 10-year period, ending on 1 January 2003. AFTA is flexible by providing the option to exclude goods temporarily or permanently from the obligation to tariff reduction (there are special exemptions for sensitive agricultural goods), and allowing new members to meet their obligations at a later date. When joining AFTA in 1995, Vietnam had committed to implement AFTA agreements on tariff reductions and removal of other trade restrictions by 2006 (Lao PDR and Myanmar by 2008, Cambodia by 2010).

With the implementation of the Common Effective Preferential Tariff (CEPT), tariffs on a wide range of goods traded within ASEAN have to be reduced to no more than 5 %, and quantitative restrictions and other non-

tariff barriers have to be eliminated. In addition to tariff reductions and elimination of quantitative restrictions, ASEAN aims at facilitating trade through harmonisation and simplification of customs procedures, streamlining customs administration, and the elimination of technical barriers to trade through harmonization of tariff nomenclatures based on the Harmonised System of the World Customs Organization and through harmonisation or mutual recognition of technical regulations and conformity assessments. However, ASEAN members do not always comply with the AFTA deadlines to lower tariffs on sensitive goods if they have a strong interest to protect domestic producers. And there seems to be a wide discrepancy between the low CEPT tariff rates and the applied rates.<sup>5</sup>

Nevertheless, ASEAN member countries aim at both widening and deepening their regional integration. With the conclusion of free trade agreements with China, Japan, Korea, and, at a later stage, possibly India, ASEAN+X could become an ever larger and more integrated Asian market combining the most dynamic developing and countries in the world. And with the Hanoi Plan of Action (1998), followed by the Vientiane Action Programme (2004) ASEAN leaders have set the target of establishing an ASEAN Economic Community (AEC) by the year 2020. The programme for a single market among the ASEAN member countries looks like a copy of the Single European Market programme, with free movement of goods, services, investment, capital and skilled labour. Yet, fundamental differences between the EU and the planned AEC remain. There are no indications that ASEAN will move from a free trade area toward a customs union and a fully integrated internal market like the European Union with supranational institutions and a single trade policy vis-à-vis the rest of the

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5 “Calculations show that only 5 % of intra-ASEAN trade has been carried out using CEPT tariff rates. Experts say that local enterprises do not bother to go through all the necessary formalities, or just do not know that their business transactions qualify for these preferential tariff rates. The authorities in countries still applying relatively high tariffs, do not bother to inform the local business sector about the CEPT, as they do not want to lose tariff revenues. In other countries, levying relatively low tariff rates, the difference between the CEPT and the ordinary rate is just too small to take the trouble anyway.” (Cuyvers, De Lombaerde, Verherstraeten 2005, 7) „Most worrying, however, has been the backtracking from original commitment by some members. Furthermore there has been little progress on the removal of non tariff barriers because there has been no agreement on what this entails.” (Soesastro 2005, 2)

world.<sup>6</sup> In contrast to the European Commission, the ASEAN secretariat does not have the capacity to enforce the rules and agreements, its mandate is confined to coordinate and facilitate ASEAN-related activities (Feridhanusetyawan 2005, 16).

ASEAN countries seem to accept that they will always be highly dependent on trade and investment relations with the rest of the world. The share of intra-ASEAN trade as a percentage of total ASEAN trade has increased from 19.3 % in 1993 to 22.6 % in 2002, but even the higher percentage shows that ASEAN countries' trade is oriented toward the global economy as its reception of investment from the major industrial countries. In view of their need to trade with the advanced industrialised countries, ASEAN countries have no interest in diverting trade from the natural patterns determined by comparative advantages through large tariff differences between intra-trade and imports from non-member states. ASEAN is not an alternative to multilateral trade liberalisation and economic integration. *“AFTA members have a strong tendency to apply the preferential tariff rates multilaterally, on an MFN basis, to non-members. AFTA tariff data show that the preferential and MFN rates are similar for a majority of tariff lines.”* (Feridhanusetyawan 2005, 18) If Vietnam will comply with ASEAN's *open regionalism*, i. e. fostering regional trade integration without excluding the rest of the world, the AFTA-induced tariff reductions will anticipate what WTO membership will bring in the field of import liberalisation.<sup>7</sup>

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6 *“As the individual ASEAN countries are reluctant to give up national economic policies vis-à-vis non-members, the AEC set-up will not include a common external tariff. This should not be too surprising as one knows that there are huge discrepancies between the member states in average tariff levels. (...) All this implies that ASEAN is not following the example of the EU and rather endeavours to establish a single market without having installed a customs union or having created some supranational authority. This is not really surprising as ASEAN members have always been reluctant to delegate power to some supranational body. In this respect it is interesting to note that ASEAN was established by a declaration and not by a treaty, meaning that ASEAN completely lacks legal personality.”* (Cuyvers, De Lombaerde, Verherstraeten 2005, 14)

7 *“Vietnam (...) maintains similar tariffs in 61 percent of all tariff lines.”* (Feridhanusetyawan 2005, 18)



### *Asia-Pacific Economic Cooperation (APEC)*

In 1989, the Asia-Pacific Economic Co-operation Forum (APEC) was formally established, encompassing 21 member countries with Pacific shores, aiming at achieving free trade among developed member countries by 2010 and for developing countries by 2020. Vietnam became member in 1998, committing itself to liberalize its trade with APEC countries by 2020. Each member country has to present Individual Action Plans (IAPs), which describe voluntary and non-binding liberalization measures. Until now, Vietnam has presented four IAPs. The one presented in 2001 is the most precise including the commitment to liberalize the conditions for joint ventures and to streamline the customs system. Although the commitments are not as binding as AFTA-requirements and lack concrete implementation plans, they are also a step towards liberalizing the economic system. Due to extreme differences between APEC members in terms of their levels of development and their economic policies, the ambitious goals set for liberalising trade and investment within the APEC seem somewhat unrealistic, and this grouping has lost importance compared to the integration programmes among Asian countries.

### *US Vietnam Bilateral Trade Agreement (US BTA)*

The US-Vietnam Bilateral Trade Agreement (US BTA) became effective in December 2001 and is regarded as a milestone for Vietnam's economic transformation and integration process. After receiving Most Favoured Nation (MFN) treatment by the US, the share of Vietnam's exports going to the American market increased significantly from 16 % in 2002 to 22 % in 2003 (CIEM 2004, 20).

In view of the WTO accession process, it is important to mention that many legal and technical commitments of the US BTA are identical or even stricter than WTO requirements. Therefore, implementing US BTA means anticipating most of the WTO requirements and should facilitate WTO accession. Nevertheless, one should not forget that after WTO accession, Vietnam has to grant most of the provisions of US BTA to *all* WTO member countries. Furthermore, Vietnam has stated not to discriminate against the European Union by US BTA, granting MFN status to European exports and investors. In ongoing talks between the EU and Vietnam, a bilateral trade agreement on the lines of the US BTA is negotiated.

### *Other integration projects*

Apart from the bilateral and regional agreements mentioned above, Vietnam has signed other agreements concerning investment promotion and protection with about 40 countries. Most of these agreements have stricter requirements than those conceded in the Law on Foreign Investment, including direct investments, portfolio investments, contract-based rights, tangible and intangible assets and intellectual property rights.

## 2.5 Vietnam's WTO accession process

Vietnam submitted the application for WTO membership on 4 January 1995. The Working Party on the accession of Vietnam was established on 31 January 1995. It is open to all WTO member states interested in Vietnam's WTO accession and bilateral negotiations on trade liberalisation. The Working Party had altogether 43 members (counting the EU as one), which have negotiated with Vietnam on its "membership package".

On 24 September 1996, Vietnam submitted its "Memorandum on the Foreign Trade Regime", which explains its trade and economic policies and institutions relating to WTO agreements in detail. The first meetings of the Working Party were on 30–31 July 1998 and 3 December 1998. Before the first meeting, members of the Working Party had submitted several hundred questions covering not only the foreign trade regime on goods, but all aspects of Vietnam's economic and political system, the treatment of state-owned enterprises and foreign invested companies, monetary and trade policies, including the bilateral or plurilateral trade agreements that may affect the competitive position of Vietnamese traded goods and the capacity of Vietnam to implement the various WTO rules and agreements. Before the first meeting, the Government of Vietnam provided a first round of answers in written form (the Memorandum, the questions/replies documents, and other unrestricted documents on the preparation of Vietnam for WTO membership can be downloaded from the WTO website). Since 1998, 14 meetings of the Working Party were held in parallel with several rounds of bilateral negotiations about the conditions of Vietnam's WTO accession took place. In 2004, the results of the question and answers process during and between the meetings of the Working Party were compiled to a Draft Report of the Working Party, which was further discussed and refined in the subsequent meetings.

Meanwhile bilateral agreements have been concluded with all major trading partners, including Mexico, Japan, China, Chile, Argentina, Brazil and the EU. In May 2006, Vietnam was able to conclude the last bilateral negotiations with the US. The accord with the US will open Vietnam's financial sector and other services sectors wider for foreign investment (foreign banks will be allowed to establish 100 per cent subsidiaries), the US will remove existing quotas on Vietnamese textile and clothing exports, but will treat Vietnam as a *non-market economy* (NME) for 12 years after accession until the end of 2018, which will make it easier to impose anti-dumping duties in case US competitors feel unfair competition from Vietnamese imports (Financial Times, 16 May, 2006, 4). However, the US has changed Kazakhstan, Russia and, recently, the Ukraine from NME status to market economy (ME) status. Depending on the progress with its economic reforms, Vietnam should be able to convince the US – and other WTO Members – to grant it ME status before 2018. The transfer from NME to ME status can be applied even to individual industries or sectors if they can prove that they operate under market economy conditions.<sup>8</sup> Vietnam did not accept the wish of the US to insert a reference to core labour standards in the agreement, which could have been used by the Americans as another justification for imposing import barriers (*Financial Times*, 26 Oct. 2006).

The last round of negotiations on Vietnam's WTO membership took place in October 2006 with intensive consultations on the final documents which were accepted by the last meeting of the Working Party on 26 October. The accession package of documents consists of:

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8 This is explicitly stated in the Report of the Working Party on Vietnam's accession to the WTO: "*Once Viet Nam has established, under the national law of the importing WTO Member, that is a market economy, the provisions of subparagraph (a) (simplified assessment of dumping cases) shall be terminated provided that the importing Member's national law contains market economy criteria as of the date of accession. In any event, the provisions of subparagraph (a)(ii) shall expire on 31 December 2018. In addition, should Viet Nam establish, pursuant to the national law of the importing WTO Member, that the market economy conditions prevail in a particular industry or sector, the non-market economy provisions of subparagraph (a) shall no longer apply to that industry or sector.*" (WTO 2006b, 66, para. 255 (d))

- the Working Party’s 260-page report on the legal and institutional framework of Vietnam for trade and related policies including the commitments Vietnam has made in these areas,<sup>9</sup>
- a 560-page list (*schedule*) of Vietnam’s commitments on goods – tariffs, quotas, tariff quotas and ceilings on agricultural subsidies, including timetables for implementation of agreed tariff cuts and other market opening measures,
- a 60-page list (*schedule*) of Vietnam’s commitments on services with the details on which type of access is given to foreign service providers in which services, and on the conditions of foreign ownership in service establishments.

At its 7 November meeting, the General Council of the WTO approved the package and Vietnam’s membership. The Vietnamese Delegation was welcomed by the Director General of the WTO, Pascal Lamy, as representatives of the next WTO member that would be able not only to benefit from the past multilateral negotiations on market access liberalisation, but also participate in the ongoing round of WTO negotiations. With its willingness to carry out the negotiations for WTO membership despite the difficult situation of the WTO after the suspension of the Doha Development Round in July 2006, Vietnam reveals its faith in the attractiveness of the multilateral rules-based trading system of the GATT and the WTO.<sup>10</sup> Vietnam will now have to ratify the deal, and become the 150th WTO member 30 days after it has informed the WTO that it has ratified the package deal. The National Assembly will have to approve and ratify Vietnam’s package deal with the WTO members to finally open the door to the WTO. It is expected that the National Assembly will ratify the agreements on December 5, so that Vietnam could become WTO member

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9 WTO News Items, 26 October 2006 (WTO website). The three documents have been released to be downloaded from the WTO website (WT/ACC/VNM/48, Add. 1, Add 2).

10 „WTO membership is not only important for Vietnam, but for the organization too. With Vietnam joining in, we demonstrate to the world that the multilateral trading system continues to show its uniqueness, comprehensiveness and attractiveness.” (Pascal Lamy: Welcome Address by the Director-General to Vietnam at the General Council Meeting on 7 November 2006.)

at the beginning of 2007, no less than twelve years after the presentation of the application.

In view of the cumbersome procedures on the way to WTO membership one might feel tempted to question the rationale of undergoing this process. But critics should not forget that the alternative would be a host of bilateral agreements with major trading nations. As a relatively small country with a small market due to its low level of economic development, Vietnam would not have much leverage to gain better conditions for its trade with larger trading nations in bilateral negotiations. On the contrary, the evidence from the large number of bilateral trading agreements is that the developed countries tend to negotiate even more concessions from the less developed countries than are on the table of WTO negotiations (“WTO+”). In addition to that, there is the systemic threat that the criss-crossing bilateral trade agreements produce intransparent conditions for international trade undermining the potential gains from trade in an open liberal trading system, in which multinational corporations can place their investment and organise their internationally integrated production according to the comparative advantages of each country involved. There is another advantage of multilateral trade negotiations in the WTO over bilateral negotiations: The WTO has become relatively transparent offering many documents to public scrutiny via its website, and there is a broad and informed global debate about the development impact of the WTO rules and agreements. What is being negotiated in bilateral negotiations is far less transparent, so that the risk for smaller and poorer countries to be treated unfairly by the rich and big countries is far greater. From Vietnam’s perspective, it makes sense to become a WTO member and contribute to the global debate and negotiations in the WTO about the future of the multilateral trading system and how to harness it for the interests of the developing countries and the world’s poor.

### **3 The new rules of the WTO and their implications for industrial policy and export promotion**

#### **3.1 The new rules of the WTO**

With the Uruguay Round (1986–94), the last multilateral round of trade negotiations in the GATT, the world trading system has changed gear from shallow toward *deeper integration*. Whereas the General Agreement on

Tariffs and Trade (GATT) provided rules mainly for border measures (tariffs, quantitative import restrictions, prevention of unfair competition through subsidised exports and through dumping by private firms of other countries), the new WTO agreements on intellectual property rights (TRIPS), on trade-related investment measures (TRIMs), and on subsidies, impose stricter discipline on a widening range of domestic economic policies. With the new Agreement on Agriculture international trade in agricultural products was brought into the domain of GATT rules and discipline, and the new General Agreement on Trade in Services (GATS) extends the rules to international trade in services including international investment of service companies and international migration of both service providers and consumers. Finally, with a few exceptions, all WTO Agreements are obligatory for developing countries as well (*Single Undertaking* of the outcome of the Uruguay Round), most of which are already WTO members or are applying to become WTO members, like Vietnam. Thus, the WTO rules and agreements are becoming the legal framework for global economic governance.

In the following, an overview is given of the new WTO framework in order to show the implications for developing countries' room for manoeuvre for industrial policies and export promotion.

The **General Agreement on Tariffs and Trade (GATT)** is still the main pillar of the WTO system and the rule book for trade in goods. Even in the area of tariffs, the Uruguay Round brought a fundamental change from shallow to deeper international economic integration of developing countries. Before the Uruguay Round, developing countries had not participated actively in GATT negotiations on tariffs, claiming that they needed high import tariffs and other protectionist measures to implement their preferred strategy of industrialization through import-substitution. The result of this non-engagement was that tariffs and other import barriers of developed countries remained relatively high especially in areas of export interest for developing countries. Therefore, during the Uruguay Round the more advanced developing countries were for the first time prepared to engage actively in the multilateral tariff negotiations by offering own "tariff concessions". Of course, most economists argue that tariff reductions are not concessions in the sense of real costs to the economy, on the contrary, by opening one's own markets to international competition encourages, a country will specialize on what it can best produce (or supply

as service) and import what it cannot produce at internationally competitive prices. Import competition will force domestic producers to increase their productivity and to improve their products, or they will have to give up and their products (or services) be replaced by cheaper/better imported goods. Nevertheless, bargaining about reciprocal tariff concessions makes sense for governments because the perspective of open export markets can win political support from export sectors over protectionist interests of import competing sectors. Recently, some economists put again emphasis on the short term costs of trade liberalisation for developing countries, especially the least developed countries, which face immediate adjustment costs when some industrial or even agricultural production has to close down due to cheaper imports and the dismissed workers and employees do not find new jobs if there is already high unemployment, whereas the potential positive effects of additional exports will show only after some time and only if new exporting activities are supported by complementary government investment in infrastructure, technological capacity development, education and market research. In this view, offering tariff reductions in trade negotiations can be seen as real concessions, and the mercantilistic bargaining over reciprocal concessions makes more sense that seen from the perspective of economic textbooks.

Developing countries had accepted, however reluctantly, the message of standard economic theory that import substitution may be good for the initial phase of industrial development, but that it will lose steam if import barriers are maintained at a high level for too long so that domestic industries do not follow the technological developments and manufacturing practices in the advanced countries and become less and less competitive with international firms. This was the experience not only of Latin American countries and India, but also of the entire socialist economic block. These countries have learned that open markets are a precondition for successful exports, at least of modern industries which need unrestricted access to state-of-the-art machines and inputs for manufacturing high quality goods for the world markets. With the overall lower tariff rates as a result of past GATT rounds and with the new active attitude of developing WTO members to tariff concessions, the countries applying for WTO accession have to follow and reduce their tariffs more than developing countries had to do under the GATT. Thus, the scope for promoting the development of new industries through tariffs and quantitative import restrictions has been reduced.

Yet, tariffs can still be raised unilaterally as long as the applied tariff rates are below the bound rates submitted to the WTO. In addition to that, Art. XVIII, C, GATT still allows *infant industry protection* for new industries through tariffs. However, this requires compensation through equivalent tariff reductions for other products (e. g. market opening for agricultural products). Therefore, developing countries have rarely used this option. They preferred to justify their import restrictions with Art. XVIII, B, which allows import restrictions to prevent a balance of payments crisis. Heavily indebted countries can still apply this article. In addition to that, there is the general escape clause of Art. XIX, which allows to protect a national industry against acute damage from increasing import competition resulting from previous trade liberalisation. Again, applying Art. XIX requires compensation through equivalent tariff reductions for other product categories. Finally, the WTO does not rule out protecting and restructuring an industry threatened by increasing import competition by means of subsidies, as long as there are no export subsidies involved.

The **Agreement on Trade-Related Investment Measures (TRIMs)** is one of the most controversial issues on the multilateral trade policy agenda. It rules out indirect import restrictions through local-content obligations for foreign (and national) investors, which oblige them to reduce the share of imported inputs in favour of inputs from domestic ancillary industries. This strategy had been implemented in the past not only by many developing, but even by some developed countries like Australia, especially in the automobile industry (Pursell 2001; UNCTAD 2003). Foreign investors were forced to invest in assembly plants in developing countries through rising tariff walls or outright import bans for finished products. When the foreign investors tried to circumvent the import ban by simply importing completely knocked down (ckd) kits of the finished automobiles which were assembled in the developing country with little (or even negative) value added, the host governments invented a new policy known as local content policy, obliging the foreign investor to raise, within a given time span, the local content of his production in the host country. The foreign investor could meet the new obligation either by expanding his production upstream, i. e. by producing more of the inputs needed inside the assembly plant in the host country, or by searching for local suppliers or components and spares, or by persuading his suppliers back home to relocate some of their production capacities to the host country in order to remain the original equipment supplier to the automobile



plant in the developing country. Now the TRIMs Agreement of the WTO puts an end to this type of forced local sourcing through investment agreements or other indirect incentives (tax incentives, differential tariff rates depending on the local content achieved). Export obligations, i. e. the obligation of foreign investors to achieve certain export targets in order to balance the import content of local manufacturing, are also banned by the TRIMs Agreement.

The brevity and vagueness of the TRIMs Agreement results from the compromise between the interests of developed countries, especially the US, the EU and Japan, in having a comprehensive agreement on foreign investment as an outcome of the Uruguay Round, and the defensive position of most developing countries who feared their national sovereignty would be curtailed by restrictions on their policies on foreign investment and their capacity to apply certain performance requirements on foreign investments for balance-of-payments purposes and as instruments of active industrial policy (local content requirements) (Greenfield 2001, Bora 2002). Many developing countries regard the transitional period of five years (seven years for least developed countries) as too short for adjusting their industrial policies, and several countries have applied for an extension of the transitional period. All acceding countries, however, had to agree to implement the TRIMs Agreement from the day of WTO accession (Brooks / Fan / Sumulong 2003, 16).

There can be no doubt that the TRIMs Agreement reduces the policy space of developing countries (and even of developed countries as the dispute settlement case between the EU and Canada as the defendant country concerning measures affecting the automotive industry shows). Whether the overall effect of the ban of TRIMs will be negative or positive from a developmental viewpoint, however, is difficult to say. It depends on whether developing countries will be able to attract more and higher quality FDI when they phase out performance requirements like increasing local content. For a balanced assessment one should keep in mind that before the TRIMs Agreement came into effect, only the larger developing countries were able to apply local content policies and other TRIMs, because their domestic markets were attractive enough for foreign investors to accept local content requirements and other constraints as entry price to the large market. With the TRIMs Agreement, this advantage of the large developing countries will disappear. All developing countries can now use

the remaining policy space with positive measures to improve the technological capacity of domestic ancillary industries, so that foreign investors are prepared to consider buying components and spares from them.

With the **Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS)** today's late industrialising countries are denied the instruments of unofficial (grey) technology transfer like reverse engineering or illegal copies that both developed and the newly industrialising countries (NICs) had used at an earlier stage of their industrial development. The driving force behind taking the TRIPS Agreement into the WTO were the interests of knowledge intensive industries producing goods with a large share of research and development (R&D) costs in total production costs (e. g. pharmaceuticals, standardised software) which can be copied easily. These industries see their patents and copyrights as their most valuable assets and are highly interested in strengthening patent and copyright protection on a global scale and in having intellectual property rights (IPRs) enforced by their governments through effective instruments like trade sanctions. Patent protection establishes a time-bound monopoly for the IPR holder, which can reduce the welfare of the society. There is a growing awareness that the TRIPS Agreement has gone too far into the direction of protecting the interests of industries inventing new products and technologies vis-à-vis the interests of the society in disseminating the new technologies for the public good. The debate on patents for Humanes Immundefizienz-Virus/Acquired immunodeficiency syndrome (HIV/Aids) pharmaceuticals has shown that there may be a public interest in having new technologies disseminated for wide usage in order to protect a public good, like health in this case.

The TRIPS Agreement is one of the most controversial issues in the debate about the justification and consequences of the deepening of the multilateral rules-based system of the WTO. Even liberal economists who defend the general move towards free trade and deeper integration of developing countries into the globalising economy have questioned the economic justification for taking the intellectual property regime into the WTO and changing the balance between the interests of the intellectual property rights holders and the public interest of free access to new technologies and ideas towards the interests of the former by extending the time given to them for exploiting the exclusive rights for their inventions (Bhagwati 2005). In view of the negative consequences for the poorest countries who

will not benefit from strengthened IPRs and only have to pay more for the utilisation of patented drugs and other technologies, prominent economists have advocated to scrap TRIPS completely (Birdsall / Rodrik / Subramanian 2005).

The problem of having to adopt a system of intellectual property rights which may not be suitable for less developed countries, is aggravated by the mushrooming of IPRs over the past decades especially in the United States, but also in the European Union. The scope of intellectual property protection has been extended and enforcement strengthened. The range of what can be protected as intellectual property has widened during the past decades. Software, business methods, geographical indications and even living things and materials have become patentable, the duration of patents has been extended and the enforcement mechanisms have been strengthened (Commission on Intellectual Property Rights 2002, 2). Excessive protection of intellectual property has become a problem for scientific progress since universities follow the trend towards patenting even basic scientific concepts, research methods and results, a general trend that is most visible in the United States. It will become more difficult to build further research on the existing state of art if the researchers have to bargain with the patent holders before they can do their own research using the results of other researchers. This can have detrimental effects on technological development even in the developed world.

The trend in the US and other developed countries to reduce the area of open science through patenting the results of university research and public research institutes will make it even more difficult for developing countries to narrow the gap to the frontier of scientific progress in the developed world. This is not a consequence of the TRIPS agreement but of the general trend towards privatizing basic scientific research in the developed world. In order to overcome the catch-up problem for developing countries, a proposal has been made to establish global funds for supporting research on issues of special relevance for developing countries (Birdsall / Rodrik / Subramanian 2005) and for negotiating a multilateral agreement on open access to basic science and technology. Such an agreement would aim at facilitating reciprocal access for the researchers of the signatory countries to the results of each other's university research and other public research, and facilitate international cooperation in basic scientific research.

The need for some ‘rebalancing’ reform of the TRIPS Agreement has been accepted in case of threats to (global) public goods. With the Doha Declaration, developing countries in need of cheap pharmaceuticals for HIV/Aids treatment were given the right of compulsory licensing and trading of generic drugs. It remains to be seen whether this is the beginning of a general relaxing of the TRIPS Agreement in favour of the least developed countries and developing countries in general. Such a readjustment will be even more justified since the industrialised countries have not met their obligations under the TRIPS Agreement to encourage and facilitate technology transfer to developing countries (Stiglitz / Charlton 2005, Srinivasan 2002).

The new **Agreement on Subsidies** distinguishes between prohibited subsidies, subsidies that can be contested and permissible subsidies. Direct and indirect export subsidies are prohibited, whereas subsidies for research and development (R&D) are allowed. Countries with a per capita income below 1000 US\$ are still allowed to use direct export subsidies. Once they have passed the threshold of 1000 US\$, they have to phase out these export subsidies within eight years. Countries that have recently joined the WTO however, were not conceded this transition period. They were asked to phase out export subsidies as soon as possible. This means that the new WTO member countries cannot follow the strategy which most of the earlier industrialising countries pursued when they complemented their infant-industry protection through high import tariffs and quantitative import restrictions with an active policy of export promotion through export subsidies. This policy mix was necessary to avoid the shortcomings of excessive import substitution strategies (as implemented by, e. g. China and India for decades). The new industries established behind high tariff walls tend to lose contact with rapid technological progress in the industrialized countries and with the level of quality, reliability and customer satisfaction required for exporting to these markets. Export subsidies were a means to compensate the negative incentives to export for industries that had developed behind tariff walls – overvalued exchange rates and limited access to imported components. These negative incentives to export will be reduced, however, with the general trade liberalisation as a result of WTO membership. In an open economy, exports no longer require direct export subsidies.

Even with the WTO ban on direct export subsidies (interestingly, the developed countries have not phased out their export subsidies on agricultural goods, and negotiations on the final date for phasing out these export subsidies have played an important role in the Doha Round), developing countries still have a wide policy space for promoting exports through technical assistance (provision of information on export markets, support for getting into contact with buyers overseas etc.) and financial support (export insurance schemes) for export marketing. Providing an efficient infrastructure and trade-related services (e. g. testing and certification institutions that help exporters to meet the widening range of product standards on developed countries' markets), and reducing administrative obstacles to international trade will be a more efficient way of trade promotion than subsidies.

With the new **General Agreement on Trade in Services (GATS)** a multilateral framework has been established for cross-border provision of services (banking, insurance, transport, software, construction, tourism, professional services like doctors or architects).<sup>11</sup> The GATS is part of the Uruguay Round package that commits all WTO member countries, including developing countries. Yet the obligation to liberalise trade in services under the GATS is relatively moderate. Every country may define the services sectors for which it wants to allow foreign providers of services access to the domestic market. There is a host of market access barriers for services, e. g. investment regulations and other administrative obstacles which have to be identified first and then negotiated with a specific request and offer approach. And this process is especially difficult when developed and developing countries negotiate concessions in services trade because they have rather different interests in getting access to each others' markets. Developed countries are especially interested that developing countries open their markets for establishments of foreign banks, insurance companies and other capital intensive service industries, whereas developing countries have an interest in getting free access to developed countries for their labour intensive service providers, e. g. construction companies and even individual services providers like nurses, doctors, architects, engineers, software developers etc. However, there is strong opposition in the developed countries against opening their labour markets to cheap

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11 The GATS and its implications for the service sector in Vietnam is not part of the present study on industrial policy and export promotion.

labour from developing countries disguised as service providers. Therefore, developing countries are justified to oppose an opening of their services markets which is not compatible with their development needs. This gives them some room for promoting their own new services companies (*infant services protection*). When they follow this strategy, they should take into account, however, that domestic service companies can be a burden for the rest of the economy if their services are less efficient and more costly than the services of foreign providers. Opening a country for international providers of essential services like telecommunication, banks, insurance companies, business and legal consultants etc. can help to raise the productivity level and export capacity of the entire economy.

Finally, the new rules and agreements of the WTO can be more effectively enforced through the new **WTO Dispute Settlement Procedure**. Decisions can no longer be blocked by the defendant country – it has to comply (at least after the decision has been confirmed by the second stage of the Dispute Settlement Procedure, the Appellate Body). Certainly, the WTO has no enforcement capacity of its own, it can only allow the winning party to impose trade sanctions against the defendant equivalent to the damage caused by the action of the defendant. This means that small countries do not have much leverage against large countries even if they have won their case in a WTO Dispute Settlement. Nevertheless, there is reason for hope: It seems that the WTO rules-based system and the Dispute Settlement Procedure is gaining credibility with every new decision so that even large countries feel obliged to accept a WTO Dispute Settlement decision and to change their policies accordingly.

### 3.2 Industrial policy space under the WTO

Recently, the debate on industrial policy under the WTO has gained momentum with the publication of new books and papers by eminent economists and economic historians showing convincingly that not only the rapidly industrialising countries in East and South East Asia had used a number of instruments for strategically promoting the development of new industries and for defending them against import competition during their learning phase, but that even the Western industrial countries had used far more active industrial policies at their early stages of development than would be allowed under the multilateral framework of today (Chang 2002;

Gallagher 2005; Stiglitz / Charlton 2006; Yong-Shik Lee 2006). If today's industrialising countries are denied to apply the same active industrial policies which the developed countries had used at their early stages of industrial development and which they still apply for protecting declining industries (e. g. until 2005, their textile and clothing industries could be protected with import quotas) and for protecting their agricultural sector which has a comparative disadvantage against efficient producers in developing countries, this creates the perception of a fundamental unfairness built into the WTO system. Developing countries knew this all the time, but they felt less affected in the old times of the GATT when they did not play an active role in the negotiations on tariff reductions and did not to offer reciprocal concessions themselves. This has changed with the Uruguay Round and the replacement of the GATT Secretariat by the WTO. In principle, all agreements are binding all WTO member states (*single undertaking*),<sup>12</sup> and a number of the new agreements do have important consequences for a widening range of trade-related economic policies thus limiting the *policy space* for all WTO member states. This is more relevant for developing countries as they were mainly using certain economic policies for developmental purposes, which are now ruled out by the new WTO agreements.

Since the failed WTO Ministerial Conference in Seattle in 1999, there is increasing criticism from developing countries and the global civil society that the Uruguay Round in the GATT had been a bad bargain for developing countries. They had accepted a number of new agreements imposing stricter disciplines for trade-related economic policies that limit their policy space for active and selective industrial policy and export promotion, against the promise of the developed countries to open their markets for agricultural products and textiles and clothing from developing countries.

In the years after the end of the Uruguay Round, it became clear that full compliance with the new agreements would entail considerable costs for developing countries before they would have any benefit from them, whereas the developed countries postponed the implementation of their

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12 Only least developed are not obliged to comply fully with the new rules and agreements, at least they are given long transition periods, e. g. for establishing their systems of intellectual property protection. To what extent other developing countries can use the escape clause of *special and differential treatment*, is still a topic for debate and negotiations in the ongoing Development Round.

obligations from the Uruguay Round – they required another decade for phasing out existing import quotas on textiles and clothing, and the promised liberalisation of agricultural markets, especially the phasing out of export subsidies, is still an issue for negotiations in the new Doha Round of the WTO.

The criticism of the unfair deal of the Uruguay Round has been supported by more detailed assessments by a number of heterodox economists and economic historians arguing that the narrowing of the policy space through the new WTO rules and agreements is detrimental for economic development through industrialization in developing countries. Orthodox economists on the other hand, counter that the new disciplines for economic and industrial policies will force developing countries to pursue more transparent and predictable market oriented policies which will result in increasing investment from both domestic and international firms and lead to higher growth rates and economic development.

The debate on the implications of the new WTO rules and agreements is fuelled by the controversial debate on the origins and ingredients of the East Asian Miracle, i. e. the exceptionally high growth rates of East Asian Newly Industrializing Countries (NICs) for several decades, interrupted only by the short interlude of the Asian crisis 1997/98. The debate has generated certain widely shared conclusions which are summarized here:

- With the exception of Hong Kong, which was a special case as Mainland China's export window to the world, all East Asian NICs did apply some sort of active and selective industrial policy, at least during the early phase of their industrial development (World Bank 1993). The vast literature on East Asian countries' development experience provides ample evidence that active and selective industrial policies did play an important role in the early phase of industrial development.
- Whether selective industrial policy has been effective in raising economic growth above the level that these countries would have achieved without selective interventions is difficult to measure due to the lack of counterfactual evidence. However, there is empirical evidence that East Asian governments have managed to stimulate industrial development, export diversification and economic growth of their countries. Some interventions were more successful than others, espe-



cially if they were performance-based, as for instance export subsidies (Bora et al. 2000, 13, 33). Many of the structural transformations occurring in these countries would not have taken place without industrial policy interventions. High tech industries in countries that had been mainly commodity exporters (e. g. Malaysia) would not have established without some form of government support. On the other hand, there are examples for failed policies, e. g. the failed automotive policies in Malaysia and Indonesia.

### **Box 1: The meaning of Industrial Policy**

There is no single definition of “industrial policy”. Recent definitions are:

*“Industrial policies comprise a variety of actions designed to target specific sectors to increase their productivity and their relative importance within the manufacturing sector.”* (Pack 2000, 48)

*“...industrial policy is basically any type of selective intervention or government policy that attempts to alter the sectoral structure of production toward sectors that are expected to offer better prospects for economic growth than would occur in the absence of such interventions, i. e., in the market equilibrium.”* (Pack / Saggi 2006, 2)

*“...restructuring policies in favour of more dynamic activities generally, regardless of whether those are located within industry or manufacturing per se. (...) The nature of industrial policies is that they complement – opponents would say ‘distort’ – market forces: they reinforce or counteract the allocative effects that the existing markets would otherwise produce.”* (Rodrik 2004, 2)

Thus, the general understanding is that industrial policy comprises selective government intervention to change the structure of industry (and the sectoral composition of the entire economy if selective intervention in favour of certain agricultural activities or services are included) from the market pattern. The objective of industrial policy is to stimulate the diversification of the economy towards higher value-added activities that generate new employment and exports.

The economic rationale for industrial policy is to correct market failures. Markets do not work perfectly if there are entry barriers due to economies of scale, which large companies enjoy as a result of large-scale mass production. Another market failure results from risk aversion of private entrepreneurs who will not invest much in research and development (R&D) of new products and new technologies if there are not sufficient guarantees that they will be able to reap the profits from successful inventions or product development. Especially at an early phase of industrial development, markets alone will not trigger off major industrial investments with economies of scale and linkages to other investments. There can be a need to coordinate investment strategies and projects in several industries each of which would not be profitable alone. A similar market

failure prevents that exports are triggered off by opening of export markets alone. The first company venturing into exports will face a number of institutional obstacles (customs procedures, convincing customers of the quality and reliability of his products) and economic risks (obtaining export credits and risk insurance), which require substantial initial investment, including the risk of failure, before exports thrive and generate a return on investment. The pioneer will avoid venturing into exports and taking the risks of pre-investment if he cannot prevent other companies to learn from his experience and start exporting with lower transaction costs and risks. This market failure is a justification for government subsidies to exports, especially during the pre-investment phase of pioneering companies (market research, risk sharing schemes etc.) These typical market failures at an early stage of industrial development and export orientation call for some type of consultation between economic policy makers and the business community in which targets are defined and complementary activities of both sides negotiated.

The East Asian type of industrial policy differs from the two other models for promoting industrial development through government interventions: In contrast to the socialist countries, East Asian NICs did not believe in the virtues of central planning and public ownership of all enterprises. They avoided the pitfalls of the ideological Cold War between central planning and pure market economy and tried to find a pragmatic compromise between the market and the state in directing industrial development and allocating the necessary resource. In contrast to the preoccupation of Latin American development thinkers with import substitution industrialization (ISI) in the 1950s and 1960s, East Asian policy makers saw no virtue in delinking industrial development from the world markets. By combining some degree of infant-industry protection with an early orientation of the new industries towards exports, they avoided the risks of excessive import substitution strategies, which undermined international competitiveness of domestic industries. When all developing countries changed their development strategy from import substitution to outward orientation and integration into the global economy, East Asian NICs were in a better position to manage a more gradual change towards complying with the rules of the game than many former socialist and Latin American countries.

- Neoclassical economists tend to deny any positive impact of industrial policy and point to examples of failed projects (e. g. Indonesia's and Malaysia's national automobile policies). They emphasise the risk of *rent seeking* by industries and individual companies benefiting from selective industrial policy measures they were able to demand from economic policy makers and bureaucrats. Neoclassical economists see the risk of misallocation of scarce resources, rent seeking and corruption as a justification for pleading neutral and generic economic policies, especially for weak governments and countries which do not have

a meritocratic bureaucracy with a strong commitment for the public good instead of pursuing selfish interests (Jwa 1999; Noland / Pack 2003).

- On the other side, there are economists who regard industrial policy of East Asian style, i. e. with its strong emphasis on promoting international competitiveness of national industries instead of protecting them from international competition as the old fashioned import substitution strategy had done, as beneficial for economic growth (Amsden 2000, 2001; Wade 2000; Westphal 2000; Lall 2003, 2004; Stiglitz 2001; Stiglitz / Charlton 2005). In this camp, there are some who argue that the impact was positive in general, however relatively small compared to other factors like political stability, a legal system with reliable property rights and effective courts for contract enforcement and transparent procedures for the settlement of disputes between companies, a sound macroeconomic framework favouring exports, good infrastructure, openness for technology imports and foreign direct investment, support for R&D as a prerequisite for technology absorption and adaptation to local conditions and upgrading, emphasis on education and vocational training, high savings rates as a special feature of East Asian people. And at the other end of the spectre of views on industrial policy there is an increasing number of heterodox economists, who argue that the good macroeconomic policy framework alone would not have triggered off the exceptionally high growth rates of East Asian countries. The advocates of an active industrial policy see a strong need for government interventions assuming that the market does not always lead to optimal outcomes. For them, the critical question is not *whether* the state should intervene in the market, but *how* to intervene in a way that accelerates economic development (Lee 2002, Jomo 2001).<sup>13</sup> *“The argument for a more balanced assessment of the contribution of industrial policy to late industrialization in the Southeast Asian HPAEs (High Performing Asian Economies) does not suggest that all industrial policy in the region has been the best possible or even consistently desirable. There have been many instances of bad industrial policy, but the existence of bad industrial policy is not proof that all industrial policy has been bad. Many of the structural transformations occurring in the region would*

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13 The Taiwanese example may be especially relevant to study : “...the Taiwanese government continues to be intensively involved in technology acquisition and in driving the small and medium enterprises to upgrade their products and processes, and in mediating the integration with the international economy. Much of the regulation and the assistance is now camouflaged to make the economy look WTO compatible...” (Wade 2000, 12).

*not have taken place without industrial policy. Good industrial policy is needed.*” (Jomo 2001, 489) Therefore, the relevant question is not, whether governments should pursue any kind of industrial policy at all, but what kind, and with what instruments and what are realistic goals? “(...) *the key issue should not be government intervention or not, although this is the current preoccupation. Instead, analytical concern should focus on appropriate government interventions in light of specific conditions and policy goals.*” (Jomo 2001, 482)

- With respect to the impact of the new WTO trading rules and agreements there seems to be a consensus that they do rule out some of the industrial policy measures and instruments like *reverse engineering*, *local content rules* for foreign investors, or *export subsidies*.<sup>14</sup> But even the critics of this trend do not expect that it can be reversed, at least in the present round of the WTO. Bilateral trade and investment agreements between developed and developing countries reveal the opposite trend towards even deeper obligations that constrain developing countries’ policy space. The interests of powerful transnational corporations in the developed world push into the direction of widening the rules for economic policies and an effective and transparent legal framework for foreign investment in all countries integrating into the globalising economy. Even the *rising stars*, China and India seem to evaluate the existing multilateral rules and agreements as beneficial for their highly successful export-oriented development strategies that are already causing concern on the side of the Western developed countries about the impact of the rising economic powers in Asia on their own *policy space* in the global economy and the institutions of global governance. Both countries use the policy space left

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14 At UNCTAD XI, Sao Paulo, June 2004, the possible conflict between the commitment to multilateral trade rules and the national policy space has been recognised for the first time in an intergovernmental consensus document. Paragraph 8 of the Draft Sao Paulo Consensus states: “*The increasing interdependence of national economies in a globalizing world and the emergence of rule based regimes for international economic relations have meant that the space for national economic policy, i. e. the scope for domestic policies, especially in the areas of trade, investment and industrial development, is now often framed by international disciplines, commitments and global market considerations. It is for each Government to evaluate the trade-off between the benefits of accepting international rules and commitments and the constraints posed by the loss of policy space. It is particularly important for developing countries, bearing in mind development goals and objectives, that all countries take into account the need for appropriate balance between national policy space and international disciplines and commitments.*” (UNCTAD 2004)

by the WTO framework in a creative way, knowing that their increasing economic power will give them more room for manoeuvre in case of conflict with the interests of Western firms.

- A realistic if sober view of the challenges of globalization sees the new WTO rules and agreements as a reflection of new trends and patterns in the global organization of industries and markets. According to this view, globalization is more than trade liberalization, it also induces a fundamental change of the global organization of industries. New transport and communication technologies in combination with new concepts of modularization of production processes have made global integration of industries possible. Multinational companies were the first to integrate developing countries into their global outsourcing and production strategies relocating standardized and labour intensive parts of their manufacturing processes to developing countries in order to benefit from their low labour costs plus additional advantages like tax rebates and other investment incentives. Smaller and more specialized firms have followed and are able to organise international production and marketing networks in which several firms work together and organize internationally integrated value chains for new products. These production networks can be even more flexible than a single large multinational corporation in organising new international production based on modularized and standardized elements of integrated manufacturing and marketing processes. Of course, the international integration of manufacturing processes requires open markets and transparent and predictable economic policies determining the costs of producing in a country. Companies organising international production networks need transparency and reliability of economic policies and trade policies in particular in all countries involved. This is the rationale for governments to enter into tighter trade agreements and become members of the WTO and negotiate ever more precise WTO agreements and rules. It guarantees internationally operating companies that their investment and cooperation strategies within global production networks will not be jeopardized by irresponsible governments who do not understand the new patterns and modalities of global industries.
- A preliminary conclusion from the present state of the debate on industrial policies under the WTO would be: Even the East Asian NICs which had applied, at an early stage of their industrial development, active and selective industrial policies with considerable success, had to change their old selective interventionist policies and adopt more generic policies which are in accordance with the legal framework of

the WTO (and regional or bilateral trade and investment agreements) and which support manufacturers in general to play an increasingly active role within the new international production and marketing networks. With appropriate generic policies (reliable legal framework, effective property rights, efficient infrastructure, promotion of R&D capacities in research centres and industry, protection of intellectual property rights, education and training), governments can help their industries to *climb the ladder* from suppliers of standardized low value-added intermediary goods to the value chains of companies in Europe or the US to producing higher value-added products within global value chains and, finally, to becoming original brand manufacturers who produce newly developed and designed products under their own brand name (Akyüz / Chang / Kozul-Wright 1998).

Latecomers like Vietnam will not be able to copy the old industrial policies of the East Asian NICs. This may not be as unfavourable as some critics of the narrowing policy space put it. In today's globalizing economy, it is no longer a realistic goal to develop integrated industrial complexes in one country. Modern high tech industries with short product cycles and high investment into R&D for new products and production technologies need the world markets as outlet to recover the investment and R&D costs as quickly as possible. Industries that are not connected to the global production networks will fall behind. Therefore, it is imperative for developing countries trying to promote industrialisation to become attractive locations for multinational companies and companies integrated into global production networks that will produce for the world markets. Several factors make a country attractive for outsourcing strategies of this type of foreign investors: Political and macroeconomic stability, a transparent legal system, an efficient infrastructure, an educated and diligent workforce, and, not to forget, local industries that can become efficient suppliers of components for the export production of the foreign firms. Thus, there is a strong case for industrial policies that encourage the development and technological upgrading of local ancillary industries as an important complement to the other policies that make a country an attractive location for multinational firms and international production and marketing networks (Hausmann / Rodrik 2002; Hoekman / Javorcik 2004).

### 3.3 Implications for Vietnam

After the first round of market reforms which triggered off a great leap forward in economic growth and export expansion driven by a commercially motivated population eager to make use of the new opportunities for establishing small enterprises and testing the markets and by a rising inflow of foreign direct investment, Vietnam will have to accomplish a second round of reforms which are necessary, first, to make its legal and institutional framework compatible with the multilateral standards for international economic transactions and second, to enhance the structural transformation of its industry so that it will be able to meet the challenges of international economic integration. The first generation of market reforms aimed at the removal of barriers against the establishment of private enterprises, foreign investment and international trade by individual enterprises. With the second generation of reforms, Vietnam will have to develop and strengthen the institutional framework for a modern open market economy, and the government will have to change its role from direct involvement in the production of goods and services through state owned enterprises (SOEs) to the more indirect role governments play in a market economy. Thus, Vietnam has to learn and implement the lessons, which other East Asian NICs had to learn in view of the fundamental changes in the world economy in which markets for sophisticated goods are increasingly being organised by international production and marketing networks, and the related changes of the multilateral trade policy framework.

As a latecomer on the global stage, Vietnam will not have much time for implementing the necessary reforms. Other countries in the region are more advanced and are also reforming their systems in order to become as open as possible to the global markets. Vietnam can study their successes and avoid some of their mistakes. If it will become an open economy with a transparent legal system and an economic administration willing to listen to the business community and to implement the reforms requested by industry, Vietnam will benefit from the economic dynamics in the neighbouring countries, where infrastructural and qualification bottlenecks (especially in China) will raise costs for manufacturing, so that international investors will search for alternative locations and find out that Vietnam has become a good and politically stable location for export processing manufacturing industries.

In view of the necessary legal and institutional reforms, the decision to join the WTO is well founded. The promise to comply with the rules and agreements of the WTO is more than the price to be paid for having better and transparent access conditions to the markets of all other WTO member states. It is good economic policy for the country itself. The WTO rules and agreements provide Vietnam's economic policy makers with a comprehensive reference guide for the necessary legal and institutional reforms. By signing international trade agreements, the government binds itself against a *policy reversal* under the pressure of protectionist and rent-seeking lobbies. As long as the government can argue that attempts by import-competing industries to roll back the reform programme would put the export interests of new industries (and agriculture) at risk, it will be able to contain the protectionist pressures. Making Vietnam's economic reforms sustainable and credible for the outside world is one of the most important effects of WTO membership. It will certify the country as attractive platform for producing components within global production networks.

Compared to the positive effect of WTO accession for Vietnam's perspectives to join the league of rapidly industrialising East Asian countries, the negative effect of a reduced *policy space* for selective industrial policies seems to be acceptable. Of course, some of the new rules like the TRIPS Agreement on intellectual property rights, or the TRIMs Agreement do reflect the business interests of multinational companies in the developed world who try to defend their leading position in the world markets based on advanced technology, management and production systems against new competitors from developing countries, especially if they get excessive subsidies or other direct support from their governments. But the same companies are the main agents for integrating developing countries into their global outsourcing strategies. If they want to find a place in the world markets for sophisticated manufactured goods, developing countries have to cooperate with the lead firms in modern industry and to comply with the rules of the game.

This does not prevent governments of developing countries from searching for *creative industrial policies* geared to promote and facilitate industrial restructuring of domestic industries and enterprises so that they become high quality ancillary suppliers to foreign investors and reliable business partners within international production and marketing networks. Most



governments, including those of Western developed countries, pursue some form of industrial policy geared to increase competitiveness of national producers. The long list of disputes between WTO member states over hidden subsidies and other industrial policy measures that distort international competition reveals the strong interest of governments in supporting national champions and national industries in general against foreign competitors. The multilateral trading rules have developed in response to unfair practices of supporting national producers at the expense of foreign producers. And the complexity of the system is an indication for the creativity of governments searching for new forms of subsidies and protectionist measures in favour of domestic industries.

The effect of the WTO rules is not to prevent a government from playing an active role in development, but to make it replace direct and selective intervention (such as import protection, licensing procedures and subsidies) with more generic policy instruments (such as incentives to attract FDI, to foster human capital formation, infrastructure development, capacity building, promotion of R&D through subsidies, research centres, universities, and trade promotion) that support firms in their efforts to succeed in foreign markets (Bora et al. 2000, 25, 33; Altenburg et al. 1998, 10–12). There is, however, no blueprint for the most effective model for a modern *developmental state* that encourages and supports the development of new industries and services that are able to meet the challenges of international competition. Each country must find a policy mix that suits best its development conditions.

If Vietnam wants to take full advantage of the global economic system, the country needs to find its own way for integrating into the global economy that is consistent with its specific institutional framework and economic conditions as well as with the requirements of the WTO. Even if the policy space for active and selective industrial policy may be more limited today than it had been for the more advanced East Asian NICs before the new WTO rules and agreements came into effect, the agenda for Vietnam's "second generation reform programmes" is ambitious enough that the government will have to mobilize all its capacities to implement the programmes in a coordinated and effective way. The major tasks the Vietnamese government will have to solve are:<sup>15</sup>

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15 The following is based on: Consultative Group (2005).

- **Reform of the legal system:** Economic legislation in accordance with the WTO rules and agreements and, what is no less important, more effective enforcement of laws, regulations and business contracts by the courts. The legal profession in particular will need a lot of training to be prepared for the new tasks (e. g. judging disputes over trade marks and counterfeit goods).
- **Reform of public administration:** Instead of direct involvement in the production of goods and services by SOEs, the economic administration has to adopt a new role in the impartial implementation of general rules, stimulation and regulation of competition especially between public and private, foreign and domestic companies. In general: increasing transparency and accountability of all levels of government and public administration, phasing out of preferential treatment of SOEs and foreign investors linked to SOEs compared to treatment of small private enterprises, establishment of a *level playing field* for all economic agents. There may be some room for industrial policy in the sense of encouraging private investment into new ventures which could be facilitated not only by venture capital provided by State owned Commercial Banks (SOCBs), but also by close cooperation and information sharing between industrial enterprises (organised in business associations) and economic administration on investment plans, and the complementary activities the government has to perform in order to facilitate innovation, especially by small private enterprises. The reform of customs administration is especially urgent in view of *trade facilitation*. Another aspect is the need for improvement of administrative performance of provinces that lag behind others: There is scope for competition between provinces, for improvement of transparency and accountability of provincial administration through publication of benchmarks and comparison of economic performance indicators and resources used for infrastructure development and attracting industries.
- **Restructuring of industry:** Equitization of SOEs is already under way, preferential treatment should be phased out, but this may need some sort of *cultural revolution* as the old personal ties between SOE managers and government officials will play a role for some time to

come.<sup>16</sup> In order to counterbalance the political influence of SOE managers, formalisation of small and medium enterprises, removal of obstacles for their growth (land rights, access to credits, support for R&D and absorption, adaptation of modern technologies, training of entrepreneurs in modern management and marketing methods...), equal treatment of foreign investors is needed most. There may be some room for industrial policy when dealing with foreign investors even if the heavy handed methods of the past like local content obligations will no longer be allowed under the TRIMs Agreement of the WTO. But the WTO does not prevent governments from consulting foreign investors about their preconditions for increasing inputs from domestic sources. The government will not be constrained to provide the necessary complementary services in terms of technology upgrading of local ancillary industries, improvement of vocational training for raising workers' capabilities in handling modern machines and performing high quality work that is required by foreign firms searching for capable and reliable ancillary suppliers to their global production and marketing networks. Provision of adequate infrastructure and logistical services would also be part of the cooperation with foreign investors and induce them, through positive measures, to raise the local content of their production. One of the most important tasks for industrial policy will be bringing Vietnam's private enterprises into closer supplier relationship with the foreign firms manufacturing for exports. They seem to be not yet prepared to obtain a major share of their inputs to export production from local suppliers and rely on imports from their technologically more advanced and experienced suppliers abroad. (Consultative Group 2005, 35). For attaining that goal, it may be necessary to encourage and support the restructuring process of the private sector in which the majority of companies are

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16 An interesting recommendation is to transform Vietnam's SOEs gradually instead of outright privatization. *"Given the political unpalatability of, and arguably large welfare losses associated with, large-scale privatization (i. e., on account of the absence of the requisite market and regulatory institutions), China and Vietnam might very well find well-regulated business groups an attractive transitional model for cultivating dynamically efficient networks that cut across ownership forms. Such networks can, under a good policy framework, help promising firms in the two countries to economize on scarce managerial skills and high transaction costs, ease risk management by providing a mechanism for mutual insurance, and accelerate technological diffusion."* (Abegaz 2005).

relatively small. So far, there is a “missing middle” of private companies producing on a sufficiently large scale so that they can become efficient suppliers to foreign firms with their requirements for timely delivery, high quality and state-of-art technology.

- **Reform of the banking system:** *Equitization* (privatisation in Vietnamese terminology) of state owned commercial banks is ongoing. There is still a need for better governance of banks and better risk assessment to avoid further accumulation of non-performing loans. A financial system in which private banks play a major role needs supervision by a government body to avoid banking crises that can entail systemic risks.
- **Development of a modern infrastructure:** Bottlenecks leading to port congestion etc. have to be removed, the necessary investment for improving infrastructure services may be mobilised by allowing private investment where possible.
- **Strengthening of technological capacity of enterprises,** stimulation of R&D in research centres and universities. According to a United Nations Industrial Development Organization (UNIDO)-sponsored report on Vietnam’s scientific and technological capacity, the country has a relatively large number of science and technology personnel and institutions. “... *there are nearly one million graduates from approximately one hundred universities or colleges spread throughout the country and some 1.3 million have attended technical training institutes.*” (Bezanson 2000, 18.) But the quality of the personnel seems to be insufficient and the S&T system not geared to support the technological upgrading of local enterprises. Industrial policy will have to focus on improving the national innovation system and strengthen the links with domestic industries.
- **Strengthening the institutional framework for quality production:** There is a need to improve the capacity of the standards organizations, of testing and certification agencies for disseminating information and offering training programmes to an increasing number of enterprises who have to understand the importance of technical standards and quality requirements as a precondition for export marketing in developed countries where the consumers demand high quality goods and

for linking to international production and marketing networks that have their own quality standards.

- In addition to the economic reforms, there is a need for **reforms of public services** in the fields of health, education and social security in order to improve the quality and provision of the services to remote regions and poorer segments of the population. With the privatisation of state owned enterprises they will have to reduce their labour force and their internal social security systems. In-firm security systems will have to be replaced by general government-backed social security systems that are open to employees from both public and private enterprises and that facilitate economic restructuring. This is even more important for a modern economy in which people move from rural areas to the cities in order to find new jobs in industry and services. With urbanisation, the family-based social security systems will erode, so that the state has to substitute a general social safety net in order to prevent growing inequalities and discontent with the evolution of the market economy.

To achieve all this, a number of reforms have to be implemented at the same time, which do not require policies, and measures prohibited by WTO rules and agreements. Whether this ambitious agenda will leave room for and require additional selective industrial policy measures is an open question. The costs of a potential conflict with other WTO member states (the WTO itself does not initiate legal proceedings against an offending member state) have to be carefully weighted to the potential benefits of such policies or measures. When Vietnamese economic policy makers consider the options for selective industrial policy left by the multilateral trading rules of the WTO and the obligations and disciplines involved in regional and bilateral agreements, they should concentrate first on the enormous tasks the government is facing with the second generation of reforms which can be implemented without conflict with the WTO rules and agreements.

## 4 Challenges for industrial policy

### 4.1 Import liberalization

#### 4.1.1 Introduction

Tariff cuts and elimination of quantitative import restrictions are one of the ‘entry fees’ countries aiming at WTO membership have to pay.<sup>17</sup> Countries joining the WTO today and in future have to accept deeper tariff cuts than in the past because of the general lower tariff levels of the incumbents who have negotiated successive rounds of tariff reductions under the GATT (the present Doha Round is the first multilateral round of trade negotiations under the WTO). With the exception of a few tariff peaks, tariffs in the developed countries for most manufactured goods have been reduced close to zero, whereas the advanced developing countries still apply higher tariffs in general, but have also followed the general tariff reductions resulting from the GATT rounds and from their abandoning the earlier strategy of import substitution in favour of a more export oriented strategy. Before joining the WTO, Vietnam will have to adjust its tariffs downward in a very short time. This will not be a major problem in principle, since the tariff levels are already relatively low for a wider range of goods, only the reduction of some peak tariffs will cause adjustment problems for the industries and producers affected.<sup>18</sup>

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17 Of course, economists view tariff reductions as advantageous for a country as a whole. The more open the economy becomes, the more it will specialise according to its comparative advantages and make use of economies of scale in production for larger export markets. The winners from improved specialization should always be able to compensate the losers. Therefore, economists advocate even unilateral market opening. The mercantilistic bargaining between two countries over “tariff concessions” can only be justified as a way of winning the support of one’s own export industries to a trade liberalisation programme.

18 “As of 20 April 2005, Viet Nam’s trade weighted average tariff was 11 per cent and Viet Nam’s simple average tariff was 17.8 per cent. The simple average tariff on major imported items was 21.4 per cent for agricultural products, 38.4 per cent for transportation equipment, 37.3 per cent for textiles, 13.5 per cent for minerals, 18.46 per cent for machinery and electrical equipment, and 8.05 per cent for metals. Tariffs ranged from zero to 60 per cent, with about 52 per cent of the tariff lines falling into the 0-5 per cent range.” (WTO 2006b, 38, para. 149)

The purpose of this chapter is to give a brief overview of the challenges Vietnam is facing with the removal of trade barriers on imports in order to comply with GATT / WTO rules. Meeting GATT / WTO requirements means making Vietnam's tariff structure more uniform, with deeper tariff for highly protective tariff levels and removal of non-tariff barriers in the coming years.

Regarding *required tariff reductions*, Vietnam has already paved the way for WTO accession through its commitments to the ASEAN Free Trade Area (AFTA) and to the US BTA. Furthermore, the average tariff level is comparatively moderate, though it has recently increased and is now in the upper range of East Asian countries. Moreover, due to its long border with China and its long coast which are both difficult to control, Vietnam is already a relatively open economy, especially for light industrial goods. However, Vietnam's tariff structure shows very high protection rates for some industries. In these sectors, the required tariff harmonization may become a major challenge for Vietnam.<sup>19</sup>

Regarding the *removal of non-tariff barriers to trade* (NTB), Vietnam has already taken important steps according to the "tariffication" rules of GATT Art. XI. Yet, "*de-facto NTBs*" in particular, are still a major problem. Therefore, a consistent *customs valuation system* and consistent and reliable *customs procedures* are needed. This might go easily hand in hand with the necessity to harmonise Vietnam's tariff scheme since less and lower tariff rates provide the ground for easier and more transparent customs valuation.<sup>20</sup>

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19 This chapter on import policy does not aim at giving recommendations about what would be an optimal tariff structure for Vietnam. Not knowing which industries will be competitive in the future, it is difficult if not impossible – and probably not advisable – to estimate how much protection might be necessary. On the contrary, the following remarks are made having in mind that priority tasks for Vietnam will be the provision and improvement of sufficient and adequate infrastructure, the development of a cost-efficient services sector and a reliable economic framework for the development of a competitive and prospering private business sector. It will then be mainly up to the market forces to decide which industries will be the most competitive ones.

20 At present, customs procedures are being discussed especially among WTO member states since industrialized countries have put the issue of "trade facilitation" on the agenda of the current negotiation round. Facilitating trade means first and foremost the implementation of transparent and reliable customs valuation and procedures for all trading partners.

In this section on GATT requirements, firstly, a general description of Vietnam's current tariff scheme, major adjustment requirements and the implications that this might have for the business sector is given. Secondly, major NTBs currently in use in Vietnam are described. Since Vietnam will have to put special effort into the improvement of cumbersome customs procedures, special attention will be given to this *de-facto* NTB. In the second section, some concluding remarks are made on the resulting challenges of import liberalisation for industrial policy of Vietnam.

**Box 2: Provisions for tariffs and non-tariff barriers to trade of GATT / WTO**

The General Agreement on Tariffs and Trade (GATT), concluded in 1947, constitutes the major legal framework of the WTO aiming at fair and equal treatment of all signatory countries and progressive dismantling of barriers to international trade. The use of measures other than duties to restrict either imports or exports is prohibited by GATT Article XI. Policy instruments to protect domestic industries, like licensing quotas, state-trading, subsidizing and non-tariff barriers to trade are prohibited under WTO law.

Hence, the commitment to cut tariffs is the central feature of the GATT. WTO member states are required to *bind* as many tariffs as possible in GATT. Bound tariffs cannot be raised unilaterally without further negotiations and compensations for affected member countries. If the bound tariff rate for a specific product category is for example 20 %, the applied rate may be lower, e. g. 5 %. Thus, there is still some room for raising the applied tariff rate up to the bound rate. The binding refers to a maximum tariff, which restricts contracting parties to allow the tariff of a particular product to exceed the GATT binding. GATT bindings are part of WTO Annex 1A (Article II of GATT), and they are documented in individual national schedules (*schedule of tariff concessions*). For goods without tariff binding any tariff rate may be charged. With the general trade liberalization under GATT and WTO, developing countries are obliged to expand their tariff bindings to new products and to bind their tariffs at lower levels, thus closing the gap between bound and applied tariff rates.

#### 4.1.2 Vietnam's tariff scheme: in need of harmonization

Vietnam's tariff structure is biased in favour of import-substituting industries, particularly those dominated by SOEs. Tariff rates are higher for manufactured products which are also produced in Vietnam – particularly for some consumer goods like garments, footwear, ceramic products and



leather goods. Selective protection is also provided for upstream industries related to textiles (silk, cotton, certain fibres) and certain intermediate goods (metal products, cements, glass).

After several adjustments, the current export and import tariff law is in effect since 1st January 1999. Regarding imports, it consists of 97 chapters and 6247 items under a six-digit Harmonised System (HS) of product classification. Based on this law, the current tariff schedule has 16 tariff bands, down from 35 in 1997. The maximum tariff rate on imported goods has come down from 200 % to around 150 % between 1997 and 2003, accompanied by some reduction in the number of lines at the top end of the distribution. By 2003, less than one per cent of total tariff lines had tariff rates above 50 %. This accounts for around 5 % of the total import value. Maximum tariff rates are concentrated in four HS chapters: HS 22 (Beverages, spirit and vinegar), HS 87 (Vehicles, other than railway), HS 24 (tobacco and manufactured tobacco) and HS 63 (worn clothing). Besides, petroleum products, cosmetics, glass and glass products are also highly taxed products.

However, the development of the current import tariff system seems to have a short-term character to solve acute problems instead of preparing for long-term commitments to trade liberalization required for WTO membership. Vietnam has not always followed a steady policy of reducing and harmonizing tariff levels. The (weighted) average tariff rate has increased from 12.8 % in 1995 to 15.7 % in 2002 (13.4 % on manufactured goods and 17.2 % on primary products) and up to 18.53 % in 2003. In addition to this slight increase, the dispersion in tariffs has also remained rather high and the decline from 131 % in 1997 to 116 % in 2002 was even reversed by rising to 120.8 % again in 2003. The first decline was caused by a reshuffling of rates in the middle range (20 % to 30 %) in favour of relatively higher rates (30 % to 50 %). Until 2004, middle and higher range tariffs of 20 % and more had been increasing again, accompanied by a decline in tariff lines between 0 % and 20 % (Athukorala 2004, 29).

The current tariff schedule is composed of three different categories of tariff rates:

- Most Favoured Nation (MFN) tariff rates are applied to imports from countries with which Vietnam has already MFN status. These countries are the European Union, Japan, most Asian countries outside

ASEAN, New Zealand, Australia and the USA. By 2002, most imported goods entered Vietnam under MFN rates (Athukorala 2004, 28).

- Preferential tariff rates apply to goods imported under the CEPT (AFTA) agreement and textiles and garments under the Vietnam-EU-Agreement.
- Normal tariff rates are usually set at 50 % higher than the MFN ones for all other countries and under all other circumstances.

Like many other countries, Vietnam applies tariff rates in a cascading manner. Lower tariff rates are applied mainly to material inputs for production such as machinery, equipment etc., whereas higher tariff rates are applied on imported finished products. Thus, nominal tariff rates do not always reflect the effective level of protection, which is higher if inputs are taxed with lower rates than finished products. In Vietnam, this is particularly the case in the production of home appliances, textiles, clothing, motorcycles, bicycles, motor vehicles and other product categories where high Effective Rates of Protection (ERP)<sup>21</sup> persist. ERP in these sectors range between 50 % and 148 % whereas all other sectors have ERP below 50 %. However, ERP for manufacturing in general has declined from 121.5 % in 1997 to 96.0 % in 2001 and 46.3 % in 2003 (Athukorala 2004, 30).

### *Required adjustments in the tariff scheme*

During the past decade, Vietnam has already made efforts towards trade liberalisation, in particular through signing AFTA and the US BTA. A brief account of liberalisation steps required under these agreements will be given below before focusing on WTO requirements and remaining adjustment requirements.

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21 The ERP is an approach to measure the net impact of trade policies on producers. Overall protection to value added depends on the relationship of output and input tariffs and the share of imported inputs in production costs. Thus, the overall tariff structure has both a tax and a subsidy element. Tariffs on the final good can be seen as a subsidy for domestic producers, tariffs on inputs as a tax on their production. The ERP measures the respective interplay of “subsidies” and “taxes” on the value added of local production: it is positive (negative) if higher (lower) tariffs are applied on finished products than on inputs.

**Regional liberalisation – AFTA:** Since 1995, Vietnam is a member of ASEAN. The centrepiece of ASEAN is AFTA, which again has the key element of the Common Effective Preferential Tariff Scheme (CEPT).<sup>22</sup> Under CEPT, Vietnam has to reduce tariffs by the year 2006 to less than 5 % on all but few sensitive items from AFTA member countries.<sup>23</sup> By 2001, the number of items on which tariffs were already reduced to less than 5 % reached 5.000. During the final period until 2006, Vietnam will have to adjust the last 1200 tariff lines. The impact of these tariff reductions on the average tariff level of Vietnam could be higher because those items to which currently high tariff rates are applied can still not be found in CEPT schemes (“sensitive items”). However, besides tariff reductions, ASEAN as a comprehensive agreement also addresses the harmonization of tariff nomenclature, customs valuation, elimination of non-tariff trade barriers, removal of restrictions on foreign exchange etc. Therefore, ASEAN membership can be seen as an important step towards WTO accession.

**Bilateral liberalisation – US BTA:** The Vietnam US BTA which is in force since 2001 has only a minor impact on trade liberalisation. Vietnam has agreed to a limited range of tariff cuts on 244 items (195 are agricultural products) with a transition period from three to six years. The average tariff level for non-agricultural products through US BTA commitments is 22.86 %.

**Multilateral liberalisation – GATT / WTO:** Regarding import liberalisation, Vietnam’s offer<sup>24</sup> for the sixth (April 2003) and the seventh (Decem-

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22 Products eligible for concessions under CEPT must be included in the inclusion list (IL) for both exporting and importing, have a CEPT tariff of 20 % or below and contain at least 40 % of ASEAN local content.

23 It consists of four categories of products for reducing tariffs among ASEAN countries. Firstly, the inclusion list (IL) comprises those products, for which tariffs have to be reduced to 0 % to 5 %. Secondly, the Temporary Exclusion List (TEL) which comprises those products that are temporarily excluded from tariff reductions and which Vietnam has to gradually include in IL. Thirdly, the General Exemption List (GEL) which comprises those goods which are totally excluded from tariff reductions and fourthly, the Unprocessed Agricultural Products (UAP).

24 Once again: For an economist, the term “offer” is not appropriate from the viewpoint of a country as a whole, since tariff reductions and import liberalization in general open the door for a more effective integration of a country into the international division of labour and international competition for both cheaper and better products and push the economy toward higher efficiency and income levels. “Offer” is only a reflection of the mercantilistic bargaining process in international trade negotiations.

ber 2003) WTO Working Party meeting includes the binding of 96 % of the tariff lines with an average level of 21 % for non-agricultural products. These offers are not much different from the status quo of the currently applied average tariff level of 18.5 %. The final outcome of the bilateral negotiations shows that Vietnam has been able to defend in principle its tariff structure with a number of high tariffs to protect some of its infant industries and sensitive agricultural products.

The report of the Working Party does not reveal the details of the bilateral tariff negotiations, it focuses on structural issues of Vietnam's import policies that are of interest to the Members of the Working Party, such as existing specific duties which should be converted into *ad valorem* duties as these are more transparent and predictable for traders (WTO 2006b, 39, para. 154). Another contested issue are tariff rate quotas for a range of products, i. e. low tariff rates for a certain import volume above which higher tariff rates are applied. They were criticized by Members of the Working Party as outmoded and trade distorting. "*Vietnam was reminded that a tariff quota system should be simple, transparent, timely, predictable, uniform, non-discriminatory and non-trade restrictive, and be administered in a way that would not distort trade or cause more burdens than absolutely necessary.*" (WTO 2006b, 41, para. 163)<sup>25</sup> Working Party Members especially complained about application of internal taxes (e. g. excise tax on automobiles) in a way discriminating imported against domestic products. "*In their view, the preferential tax treatment for domestic producers was inconsistent with the national treatment principle of Article III and should be abolished prior to accession. These Members sought commitment from Viet Nam that it would equalize the excise tax rates on these products by the date of accession and that from this date Viet Nam would apply its taxation measures in full compliance with Article III of the GATT without affording protection to domestic production.*" Interestingly, the Vietnamese delegation defended the application of discriminatory internal taxes as an instrument of industrial policy for promoting the development of a national car industry: "*As for motor vehicles, he (the repre-*

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25 It should be noted however, that developed countries also apply tariff quota systems for their preferential duties offered under their General Systems of Preferences (GSP) to developing countries. For sensitive products, the application of the preferential rates is often limited to a certain import quantity. Once the tariff quota is exceeded, the MFN (normal) duty is applied even for imports from developing countries.

*sentative of Viet Nam) noted that the manufacturing of automobiles was still an infant industry in Viet Nam. To support this sector, preferential excise tax rates had been granted to automobile manufacturing enterprises when investment licenses had been issued. However, as a compromise between the need to support this industry and the potential negative effects that could result from the imposition of lower excise tax rates, Viet Nam had agreed to phase-out the excise tax incentive granted to domestically-produced automobiles by the end of 2006.” (WTO 2006b, 49, para. 190)*

It was mentioned during the Working Party negotiations that the still existing high tariffs for some product groups contribute to “rampant smuggling” which would put officially declared goods paying high duties at a competitive disadvantage with the same smuggled goods (WTO 2006, 63, para. 245). Thus, with illegally imported products from China there is already *water in tariffs*.<sup>26</sup> The implementation of the AFTA / CEPT scheme has lowered average tariff levels slightly. On the other side, Vietnam’s tariff structure does not yet reflect these average levels. The average tariff level of the last seven countries joining WTO ranged from 4.8 to 8.9 %, and the average tariff level on industrial goods among all WTO members is only 3.5 %.<sup>27</sup> Furthermore, and most important from this point of view, Vietnam’s protection scheme shows some very high peaks in specific industries (e. g. garment, textiles, motor vehicles) leading to a high dispersion in tariffs. Being forced to cut tariffs in these industries by 50 % and more in the near future due to WTO accession may lead to severe adjustment problems for some industries.

Summing up, one can say that even with reduced and simplified rates, Vietnam’s tariff scheme still leaves much to be desired in terms of harmonization. Tariffs of WTO members are considerably lower and the dispersion rate of Vietnam’s tariff scheme is causing concern. Furthermore, negotiating tariff cuts and transition periods is much more difficult

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26 “Water in tariffs” on specific items means that the de-facto tariff level on certain (mostly light industry) products is lower than the officially applied tariff rates suggest. Thus, the domestic product price is already lower than the price that the officially required import duties on it, plus the market price, would come to (Athukorala 2002, 19).

27 Generally speaking, average tariff rates are less than 20 % in most countries, although they are often quite a bit higher for agricultural commodities. In the most developed countries, average tariffs are less than 10 %, and often less than 5 %. On average, less developed countries maintain higher tariff barriers, but, for many countries that have recently joined the WTO, tariffs have recently been reduced substantially to gain entry.

for countries acceding the WTO today and in future, since overall tariff levels have come down considerably.

*A note on the fiscal impact of tariff reductions*<sup>28</sup>

A major concern for the Vietnamese government with regard to tariff reductions for its WTO accession is whether and to what extent this will have an adverse impact on the state budget (Cuong 2004, 18–19).<sup>29</sup> A single reduction of tariff rates would only lead to decreasing tax revenues if the volume of imports remained unchanged. But when protection is reduced, the volume of imports will probably increase and broaden the domestic tax base. Thus, government's revenue may even increase. Moreover, reduced tariff rates will diminish incentives for informal trade and thus reduce the losses from tax evasion.

**Box 3: Yarn and textiles industry**

Vietnam's textile industry profits from the comparatively low wages. However, labor costs are less important in this highly capital-intensive industry. The level of technology in this industry tends to be lower in Vietnam than in competing countries. Thus, the overall productivity tends to be low, design capacities are limited and only a small spectrum of products can be produced in Vietnam. In spinning, only short staple yarns are competitive with imports. Long staple yarns have to be imported. In the textile industry and in dyeing, the machinery standard is still quite low. Only about 40 % of the requirements for garment exports can be produced locally by suppliers and the revenue from exports of textiles and yarn is low.

Production of textiles with export quality is limited to some FIE. They are encouraged to export through government incentives in order to prevent excessive competition with the local textile industry (mainly state-owned enterprises). The industry is protected by high tariff rates of up to 50 %. Similarly high tariff rates up to 40 % are applied on raw materials like silk, cotton, wool and vegetable textile fibers. However, joining AFTA has already increased competition in this industry and by 2006, tariff rates have to be reduced to 5 % within the CEPT

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28 This sub-section does not aim at giving a full assessment of the implications of import duty reductions, tax changes and the development of import quantities since this would go beyond the scope of this study. A detailed analysis is provided by Athukorala (2004, 50).

29 Import and export duties count for an estimated 19 % of government's budget in 2003.

scheme. WTO accession will probably further increase competition, among others because upstream industries are weak (e. g. spinning). Policy measures to balance the disruptive effects of higher competition should aim at connecting the development of the textiles industry to the garment industry, since the garment industry shows higher competitiveness on international markets. Policy measures in this industry should allow private enterprises to make their own investment decisions rather than prescribing the structure of investment.

### *Implications of adjustments in the tariff scheme for industries*

Of course, the reduction of tariff levels will result in stiffer competition from cheaper or higher quality imported products. Both, private sector SMEs and SOEs will face this challenge. But import substituting FIEs will also face the challenge from cheaper imports once tariffs will come down to international levels. However, implications and resulting challenges differ among industries.

#### **Box 4: Garment industry**

The garment industry is characterized by labour intensive production. Therefore, foreign investors were attracted to produce garments in Vietnam by its large low wage labour force that can be trained very quickly. This led to a rapid increase in production and exports in recent years. Vietnamese garment exports can compete with those from other countries in quality and price. However, this industry is – like in many other successful garment exporting countries of the region – mostly processing imported textiles into finished garment exports. Particularly among private enterprises, difficulties exist in the management of designing, material purchasing, production process and quality control. These factors level out the advantages of low labour costs to a certain degree. Therefore, it is questionable whether the competitiveness of this industry will be sustainable in the future. In the garment sector, product cycles are becoming shorter and there is increasing competition through rapidly changing fashions. To remain competitive, Vietnamese enterprises would need to invest in technology, marketing etc.

The present maximum tariff rates for garments and apparel are at high levels around 50 %. In 2002, on HS 63 (other made-up textile articles) even an import tariff of 100 % was applied. The required lowering of these protection levels will further increase competition in this industry. However, competition is already increasing due to illegal imports from China. In any case, an important ingredient for further development of this industry will be training of skilled labour, improvement of management capacities, technology upgrading, improvement of quality control and increasing productivity. Furthermore, local value added needs

to be increased through improved fashion design and product development. In addition, concentrating on the domestic market could support further development since the demand of textiles is still low in Vietnam. A transparent and flat tariff rate system might encourage these changes.

Enterprises are relatively well informed about the upcoming changes. However, the majority of them expect that Vietnam, being still a relatively poor developing country, will be able to negotiate longer implementation periods for lowering tariffs that are necessary to protect industries. They fear increasing import competition resulting from lower tariff rates. Competition from China with its low cost mass production is regarded as a major challenge. Most SOEs already feel the competition from increasing numbers of private enterprises in Vietnam and also through the step-by-step implementation of ASEAN / AFTA and US BTA. Most of the enterprises say they try to meet these challenges through the production of higher quality goods in their respective field. This can be observed especially for the garment and footwear industries. Downstream industries, of course, expect to improve their competitiveness through lower prices on imported inputs.

Generally speaking, smaller private enterprises are expected to be more flexible and thus to have less problems with adapting to higher competition levels than bigger enterprises, especially state-owned enterprises. The reactions to ASEAN / AFTA membership and to the US BTA have already shown this. In addition, this assessment is supported by the observation that there is already an increase in competition in Vietnam due to widespread smuggling.

However, although differing from one industry to the other, it can be said that the overall competitiveness of Vietnamese enterprises (both, SME and SOE) is still quite low (UNDP 2000, 6). The size of most industrial enterprises is relatively small. Many goods produced in Vietnam are simple, with still rather low quality due to a low level of technology and outdated equipment. The productivity of Vietnamese enterprises is lower than in other countries in the region and the value added remains small (around 20 %). All this is to a large extent caused by a lack of finance and inconsistent government policies that do not provide the necessary reliable business environment.



In addition, one can conclude from the interviews in the business sector, that time consuming and cost intensive customs procedures are another obstacle for the development of a vigorous private sector engagement in trading. Therefore, customs procedures will be discussed in detail in the following section.

#### 4.1.3 Non-tariff barriers to trade in Vietnam: obstacles through de facto NTBs

There is no comprehensive and detailed list of non-tariff measures (NTBs) applied in Vietnam. This section sketches briefly some of the NTBs that were mentioned in the interviews with businesses and have a direct influence on them.

**Quantitative restrictions (QRs): import quotas and licenses:** Vietnam has reduced the use of QRs substantially. At present, only petroleum products and sugar are still subject to licensing while the government has committed itself to lifting quotas on sugar imports by 2005. SOE dominate in imports that are regulated by QRs because only few private enterprises are able to pass the strict and steadily changing registration procedures.

**Foreign exchange regulations:** Due to a favourable balance of payment situation, foreign exchange controls have been loosened in recent years. The foreign exchange surrender requirement for trading businesses, which was implemented in 1998 by the State Bank of Vietnam, came down from 80 % in 1998 to 50 % in 1999 to 40 % in 2001. In 2004, businesses had to transfer 40 % of their foreign exchange earnings into their accounts within 15 working days of transfer of these funds. In 2000, the foreign exchange balancing requirement for FIEs was relaxed, too. FIEs are now able to purchase foreign currency from domestic banks to repay loans obtained from offshore banks. However, although officially all firms are entitled to buy foreign exchange from banks, in practice, only large firms, mostly SOEs, receive foreign exchange from state-owned banks.

**Non-automatic licensing:** At present, there is no legal discrimination against domestic private enterprises and FIE through non-automatic licensing. Any formally registered enterprise that is also registered for foreign trade can import and export goods that are not on the list of “special” goods (commodities with import quotas, prohibited commodities, com-

modities under government management and commodities under specialized management, e. g., automobiles, motorcycles, steel, writing and printing paper, cement, beverages and fertilizer). This goes back to the Government's Decree 57 of 1998. Since then, all businesses are allowed to trade the goods registered in their business. However, enterprises still have to register export/import goods to receive trading codes from the province or municipal customs office. Moreover, firms are only allowed to trade in commodities registered in their business license. This prevents them from reacting to changing market conditions by moving from one kind of business to another without approval. Mainly private SMEs stated that this means a considerable loss of profit, because they cannot take decisions about imported items on demand. Reduced flexibility is a serious disadvantage for the competitiveness of Vietnamese enterprises.

**De-facto NTBs:** Administrative rigidities and delays in the customs administration have continued to remain an important de-facto NTBs. Customs procedures are time consuming and raise transaction costs of enterprises.<sup>30</sup> These costs arise not only through delayed customs procedures but also through unofficially required extra payments, which seem to be a common practice. Although some progress has been made through the new Law on Customs Valuation, which is in force since January 2002, customs procedures are still quite cumbersome and hurt private enterprises disproportionately. Since these difficulties were mentioned in most of the interviews as main obstacles for importing, special attention should be given to this topic.

#### *Removal of non-tariff barriers to trade*

For the phasing out of NTBs, some important steps have already been made by the Vietnamese government committing itself to ASEAN and US BTA. These adjustments will be outlined briefly before presenting the WTO requirements.

**Regional trade liberalisation – ASEAN:** The CEPT requires Vietnam to remove all NTBs by January 2009. Vietnam is already requested to list all

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30 In processing imports of goods, Vietnam's Customs still requires a range of documents such as invoices, bills of landing, customs declaration, packaging protocols, purchase contracts with price lists included, quotas granted, specific licenses like licenses for temporary imports and re-exports, document of exemption of tariff, etc.

quantitative restrictions (QRs) currently in use on a yearly basis. In 2001, the government issued a trade management mechanism for 2001 to 2005 under which it proposed to abolish several NTBs. Furthermore, ASEAN obliges Vietnam to calculate the customs value in accordance with the Customs Valuation Agreement (CVA) by the year 2000. However, for a full implementation of the CVA, Vietnam still needs training for the customs staff. Thus, only the Harmonised System (HS) has been implemented in 2000.

**Bilateral trade liberalisation – US BTA:** In Annex B1, B2 of the US BTA, Vietnam commits itself to remove all QR on imports of 69 agricultural products within a period from 3 to 5 years after the BTA has come into effect. In the case of sugar, a delayed period, which extends up to 10 years, was accepted. Furthermore, through Chapter I, Art. 3(4) of US BTA Vietnam has to adopt the CVA. In addition, the general transparency provisions of US BTA go beyond WTO requirements.

**Multilateral trade liberalisation – GATT/WTO:** After accession to the WTO, all NTBs will have to be eliminated in accordance with GATT Art. XI. Of course, this does not mean that Vietnam cannot apply the necessary safeguard measures to protect its economy, but under the strict WTO rules for reversing trade liberalization. Furthermore, Vietnam has to implement the CVA in its national legislation. Then, tariff calculation based on the transaction prices will be more precise.

However, Vietnam has applied for an extended transitional period to fully implement the CVA because the required experience, expertise, knowledge, technical facilities, and equipment seem not yet available in Vietnam. Nevertheless, first steps have been made through the new Law on Customs Valuation. It introduces the internationally required Transaction Value as a basis for the valuation of imported items according to WTO law. Yet, the new law lacks some important specifications. Since six additional valuation categories have been introduced as alternative means of valuation instead of valuation standards with different priorities, the Vietnamese valuation system does not yet fully comply with WTO standards. As necessary transparent valuation rules and procedures are not yet implemented, customs offices still provide fertile ground for arbitrary classifications.

*De-facto NTB: customs valuation and procedures*

In theory, the Law on Customs Valuation sets only one tariff rate for a certain item. But in practice, different tariff levels are applied to the same product in different provinces<sup>31</sup> due to the fact that customs offices in the provinces work rather “independently”. Thus, a predictable environment for investment in import-export business is missing.

Furthermore, cumbersome customs procedures were repeatedly mentioned as a core problem for enterprises in Vietnam. High administrative costs for delayed and opaque certification and licensing procedures are still a difficulty, especially for private and foreign invested enterprises (see Appendix: Table 2; cf. Perkins 2001, 261). In the interviews, it was repeatedly stated that “*it all depends on the officer in charge*”. Unofficial fees are said to be common practice.<sup>32</sup> For companies producing for the local market, extra-payments and delayed delivery from customs offices were mentioned in particular when asked for difficulties with importing. Companies producing only for exporting face less administrative difficulties. But still, the administrative costs are quite high due to very detailed verification requirements for the duty drawback regulations. This is especially true for the textile industry where every single piece of fabrics added to the export product has to be verified and approved by the customs office. Although foreign investors do not assess these difficulties as a serious disadvantage for increasing investment in Vietnam compared to other countries in the region, these administrative requirements represent a considerable disadvantage for Vietnamese enterprises in terms of competitiveness on international markets and hinder the development of the private business sector.

Therefore, many companies would like to see better-qualified staff at the customs offices and more efficient control and enforcement mechanisms.

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31 One entrepreneur of a FIE reported that he has to pay three different tariffs for the same item in three different ports with a range from 0 % to 10 %.

32 The following “standard” unofficial fees were reported for the footwear industry to process income shipments. According to Boye (2002), in 2002 US\$ 20 for clearing a 20 foot container, US\$ 40 for a 40 foot container and US\$ 100 late inspection fee. According to another study conducted in the garments and textile industry by the Institute for Market and Price Research in 2002, customs procedures make up for the second most difficult task for enterprises after duty drawback procedures (see Appendix: Table 2). This resembles the perceptions that the interviewed businesses contributed to the present study.

Some of the interviewed government institutions are aware of the need for additional training of customs officers in order to fully implement the new valuation system, too. Furthermore, especially FIEs see some difficulties due to insufficient technical equipment as well as capacity constraints of ports and port facilities.

In addition, it was often mentioned that many SMEs and also FIEs do a large share of their trading through bigger enterprises, mainly SOEs. This is caused, on the one hand, by foreign exchange regulations and by the above-mentioned rigidities through non-automatic licensing regulations on the other. This third party trade leads to delays for the production and additional costs through fees of 7 % to 10 % that are normally charged for these transfer services. This again represents a disadvantage for international competitiveness of Vietnamese businesses. Furthermore, these conditions are another obstacle to the development of a thriving private business sector.

Summing up, a quick improvement of customs procedures is needed – first, through the consistent implementation of the CVA and simplified tariff structures and second, through additional training of staff and restructuring of customs offices. Furthermore, improved technical facilities are needed. In many of these fields, multilateral development co-operation can (and does) offer technical assistance and training.

The problems of customs valuation were discussed at length at the meetings of the Working Party on Vietnam's accession to the WTO. *“Some members noted that Viet Nam's customs procedures were complicated and at times unpredictable depending on the discretion of customs officials.”* (WTO 2006b, 63, para. 245) The Vietnamese delegation replied that an action plan for the implementation of the Customs Valuation Agreement was implemented in order to reform Vietnam's customs procedures and bring its valuation system into conformity with the Customs Valuation Agreement. It was confirmed that *“from the date of accession, Viet Nam would fully apply the WTO provisions concerning customs valuation (...). Viet Nam would ensure that any customs valuation method to be applied would be in accordance with these WTO rules.”* (WTO 2006b, 61, para. 238) However, both *“customs officers and the business community needed training to use the new valuation procedures.”* (Ibid. 59, para. 228)

#### 4.1.4 Challenges for Vietnam's industrial policy

Vietnam's industrial policy has relied mainly on trade policy instruments. *Infant-industry protection*, i. e. a temporary closure of the domestic market in order to provide newly developing industries with the necessary learning phase for becoming able to compete successfully with imports and on export markets has been the first stage of industrialization in most countries of the world (Chang 2002). Vietnam as a latecomer in industrialization faces the twin challenge that neighbouring countries have already captured major shares of regional and global markets for a wide range of manufactured products on the lower and medium technology level that newly industrializing countries can command, making it difficult for new entrants to find their market niches without active government support, which, however, may not be offered in the same way and with the same simple but effective instruments as the East Asian Miracle countries applied at their early stages of industrial development. Today, WTO rules and agreements restrict the use of protectionist trade barriers and other instruments of selective industrial policy and export promotion. Thus, Vietnam's industrial policy is faced with the challenge of replacing traditional protective instruments like high tariff rates and NTBs with WTO compatible industrial and trade policy measures to support domestic industrial development.

Vietnam will have to remove peak tariffs on specific industries like for instance motor vehicles, garment and textiles and the traditional heavy industries like steel and cement. It remains to be seen what transitional arrangements Vietnam will be able to negotiate for some strategic industries like automobile industry where the interests of international investors, who had established auto assembly plants in view of the import protection provided, might also call for a gradual liberalization process. The major challenge for the Vietnamese government will be to develop appropriate policy instruments to avoid disruptive effects of the removal of industry protection and the change in industrial policy-making. The major task will be to shift industrial policy to complementary measures and policies instead of specific interventions. These could include, e. g.:

- Provision of an efficient infrastructure, on the one side through road building, ports and railways etc. and on the other side through a non-SOE-biased service sector. An efficient infrastructure could facilitate

enterprises to grow and profit from economies of scale, for instance in research and development (R&D), marketing etc.

- Support to R&D within the business sector to gain competitiveness in faster changing product cycles through technological innovation.
- Support for the formation of industrial clusters and the formation of business networks, first and foremost through existing intermediary institutions like business associations or Vietnam Chamber of Commerce and Industry (VCCI) etc. The competitiveness of Vietnamese businesses could increase through this form of concentrated interaction between suppliers, services and supporting institutions and even universities.
- Support for human resource development, particularly in the formation of high skilled labour with specific qualifications.

However, these modern industrial policy instruments that will have to replace industry protection can only be implemented efficiently if the Vietnamese government is able to develop a level playing field for private and state-owned and foreign invested enterprises. Uneven treatment in tax and tariff policy or in customs procedures needs to be removed. Then, the focus should lie on the provision of a reliable economic framework for private companies, state-owned enterprises and foreign invested enterprises. This includes developing adequate adjustment policies to balance disruptive effects of import liberalisation on the labour market or the banking sector.

It becomes clear that intermediary institutions at the meso level will play an important role in the process of policy change. For an efficient implementation of most of the instruments mentioned above, the government needs to rely on suggestions from the enterprises concerned through their respective network like business associations etc. Otherwise, a trial-and-error search process for appropriate alternative measures of industry support instead of protection would probably impose high extra-costs. Hence, it seems to be obvious that the Vietnamese government needs to support intermediary institutions. Industrial and trade policy instruments can be improved and adjusted more efficiently with the integration of meso level institutions channelling information from the business sector to the government and vice versa.

## 4.2 Phasing out of trade-related investment measures

In many developing countries, governments used to invite foreign investment in industries on condition that the foreign companies committed themselves to gradually increase the utilization of local inputs (local content requirements) within a given time frame of some five to ten years, and/or that they accepted the obligation to export a certain proportion of their output (trade balancing requirements). These requirements were regarded as effective instruments to encourage the development of domestic ancillary industries and to have a positive effect on the balance of trade, but they affect international trade in several ways (WTO 1999, 77). An obligation to increase the value of domestically produced inputs may prevent or limit the use of imported inputs. An obligation to export may handicap (foreign) producers who are confronted with competition in the export markets of goods that may be only exportable because of dumping or subsidising measures. Therefore, during the Uruguay Round an agreement was negotiated that prohibits such trade-distorting measures. As a result, the Agreement on Trade-Related Investment Measures (TRIMs) was signed and became effective on 1st January 1995.

The purpose of this chapter is:

- to explain what measures of localisation policy are no longer allowed under WTO law and have to be phased out,
- to sketch the challenges for Vietnam's industrial policy,
- to give an illustrative example for TRIMs applied in Vietnam (the automobile industry), and
- to make recommendations on how to reach the goal of supporting the domestic ancillary industry in conformity with WTO law.



### 4.2.1 The Agreement on Trade-Related Investment Measures (TRIMs)

Although it is only five pages long, the TRIMs Agreement has become a central issue for developing countries in the WTO. Its main objective is to reduce barriers to investment and trade and make investment conditions more favourable, transparent and predictable. The TRIMs Agreement explicitly prohibits member countries to make the approval of foreign investment conditional on compliance with national laws, policies or administrative regulations that favour domestic over imported inputs. Local content requirements are prohibited because they are contrary to the obligations of the national treatment principle (GATT Article III). Foreign exchange balancing restrictions are not allowed because they violate the prohibition of quantitative restrictions (GATT Article XI). Since trade-related investment measures have been applied by many developing countries (and even developed countries like Australia and Canada) especially in the automobile industry, this industry will be mainly affected by the TRIMs Agreement.

<b>Table 1: Illustrative list of TRIMs inconsistent with GATT articles</b>	
<b>GATT provisions</b>	<b>Inconsistent measures</b>
Article III: National treatment	Local content requirements – <b>a certain amount of inputs in production should be of local origin</b> Trade-balancing requirements – <b>imports are restricted or are linked to the amount of exports</b>
Article XI: Prohibition of quantitative restrictions	Trade-balancing restrictions – <b>as above</b> Foreign exchange balancing restrictions – <b>limiting the availability of foreign exchange for imports to a proportion of foreign exchange earned by exports or otherwise transferred</b> Domestic sales requirements – <b>a certain proportion of production is reserved for the domestic market</b>
Source: World Trade Organization (2000a, 56)	

The TRIMs Agreement does not define explicitly what a trade-related investment measure is, but it provides an illustrative list of measures that are inconsistent with GATT articles.

The lack of a precise definition has led to considerable disagreement as to whether or not certain measures are covered by the agreement. A distinction can be made as to whether a measure is “trade-related” or an “investment measure”. In a third step one has to examine whether the measure is inconsistent with the provisions of Article III and thus violates the TRIMs Agreement. A WTO Dispute Settlement Panel on “Indonesia – Autos” had to investigate these problems (WTO 2004a, 3). Concerning the definition of “investment measure” the Panel stated that the TRIMs Agreement is not limited to measures taken specifically in regard to *foreign* investment. Therefore, the agreement is ownership neutral. It simply addresses trade-distorting policies, regardless whether they are targeted at foreign or domestic companies. Moreover, even measures, which are not clearly defined as “investment measure” but have a significant trade-related impact on investments, are also subject to the TRIMs Agreement. Concerning the definition of “trade-related”, the WTO Dispute Settlement Panel on Indonesia’s national car policy stated that especially local content requirements favouring the use of domestic products over imported products have the same effect as other barriers to imports and therefore are inconsistent with the TRIMs Agreement.

#### 4.2.2 WTO dispute settlement on TRIMs

Until now, in the TRIMs area some 16 requests for consultation were initiated. Three of the cases proceeded to the next stage of establishing a Dispute Panel. It should be noted that in each case the complainant listed other policies in addition to those that were claimed to be inconsistent with the TRIMs Agreement. This is an important point because it reveals the use of multiple types of measures in the context of general industrial policy objectives as opposed to an isolated or targeted use of intervention. (Bora 2002, 171)

The WTO Dispute Settlement case on Indonesia revealed two aspects: First, local content requirements were identified as trade distorting and, therefore, have to be phased out. Secondly, a WTO member state has to respect and implement all WTO agreements (with very few exceptions).

**Box 5: The WTO Dispute Settlement case against Indonesia on TRIMs**

The WTO Dispute Panel case on Indonesia demonstrates how Indonesia's plan to develop a national automobile industry was affected by WTO law and how the Dispute Panel interpreted the measures applied by Indonesia.

The main reason for the complaint against Indonesia was its tax and tariff system concerning completely built-up units (CBUs) of imported motor vehicles. Products entering the country were subject to an import duty rate and when the product was sold it was subject to a sales tax. These taxes were not the problem, but the Indonesian scheme allowed an exemption from these duties on the basis of the local content ratio. Moreover, an agreement between an Indonesian company (PT Timor Putra Nasional) and a Korean company (Kia) gave preference to imports of CBUs from the Korean company.

In 1998, the European Community, Japan and the United States complained about the discrimination in favour of imports from Korea, the discrimination of imported goods in favour of domestic goods and the bias in the tax system in favour of domestically produced automobiles. Moreover, they complained about violations of the Agreement on Subsidies and Countervailing Measures (SCM) and the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS).

The panel decided that the measures in use in Indonesia violated various Articles of both the TRIMs Agreement and the GATT, whereas the SCM and TRIPS Agreement were not violated seriously. Since no consensus could be reached on how to implement the ruling, the parties agreed on an arbitrator who decided a 12-month implementation period for reconciling Indonesia's legislation with WTO law. In July 1999, Indonesia informed WTO members that it had eliminated the inconsistent measures in compliance with the panel's ruling.<sup>33</sup>

Source: UNCTAD (2000, 41)

33 It should be noted that TRIMs can be misused as any selective industrial policy measure for rent-seeking purposes. This has been conceded even by a strong critic of the TRIMs Agreement. "*The fact is that TRIMs often operate as a form of corporate welfare for local capitalists. For example, Indonesia's National Car Program was ruled a violation of the TRIMs Agreement. Yet the local content policies and tax exemptions involved primarily benefited President Suharto's youngest son, Tommy, who owned the local auto company PT Timor.*" (Greenfield 2001, 7.) In India, the national car project Maruti-Suzuki had been given to Indira Gandhi's elder son, Sanjay Gandhi.

The acceding countries were not conceded long transitional periods for adjusting their policies toward foreign investment, and with the USBTA and in the negotiations on WTO accession, Vietnam has already accepted to phase out all existing TRIMs.

#### 4.2.3 Implications of the TRIMs Agreement for industrial policy

Developing countries often argue that local content requirements are vital for their development, mainly because of three reasons: Firstly, it encourages the use of domestic inputs, which means saving scarce foreign exchange. Secondly, it fosters the creation of additional domestic employment. Thirdly, it stimulates domestic economic activity in general and forces foreign investors to search for local suppliers and to help them meeting their technology and quality requirements which are those of the export markets. Thus, TRIMs had been widely applied as a tool for promoting the development of local industries. The Vietnamese government stated in a similar way: *“The main purpose of introducing local content requirements in Vietnam is to promote the parts industry, to upgrade technology, to improve quality and to reduce production costs of automobile, motorcycle and mechanical-electric-electronic products; to enhance capacity of production from local raw materials.”* (WTO 2001a, 8) Therefore, many developing countries see their industrial development restricted by the TRIMs Agreement.<sup>34</sup>

The TRIMs Agreement does not rule out any industrial policy. However, it requires a radical change of investment-related policies – governments have to find other measures and incentives to build up a competitive ancillary industry without being able to protect it with high tariffs or import quotas against competition from the original component suppliers in the home country (or from third countries) of the foreign investors.

Since 1995, the Vietnamese government has pursued a localisation policy, including two programs and various incentives to build up an ancillary industry (WTO 2001a, 1): The Localisation Program, the Domestic Raw

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34 Pakistan e. g., asserted that TRIMs conformity might be contrary to its development interests; opening the economy to import competition would hinder the country from exploiting domestic resources optimally or from promoting transfer of technology, employment, and domestic linkages (Bora 2002, 173).

Material Development Program and two kinds of incentives: First, incentives in the form of digressive import tariff rates which decrease with the rising level of local content an importing company has reached; second, incentives in the form of corporate income tax the rate of which goes down with rising local content level.

There are local content requirements for three industrial sectors:

- automobile manufacturing and assembling projects,
- motorcycle manufacturing and assembling projects,
- mechanical, electric and electronic products assembling and manufacturing projects.

Up to December 2001, about 100 enterprises had registered to implement the localisation program, of which 64 % are FIEs and 36 % are local companies. These enterprises had registered local content ratios for 700 products, most of which are spare parts for motorcycles, electronic products, refrigerators and air-conditioners as well as household appliances. Apart from the localisation policy, investors in some industries were obliged to export a certain proportion of goods as a precondition for the investment license, e. g. in the bicycles, motorcycles, textiles and garments industries. This requirement was phased out in 2004.

#### *The current legal framework in Vietnam*

Various laws and regulations are relevant to investment in Vietnam: the Law on Foreign Investment, the Law on Domestic Investment Promotion and other legal documents, e. g. Decree No. 24/2000/ND-CP of 31st of July 2000 spelling out in detail the implementation of the Law on Foreign Investment in Vietnam.

Localisation policy measures are imposed on both FIE and local enterprises on a non-discriminatory basis. However, the laws do not treat businesses equally in terms of investment procedures and forms, management and incentives, etc. Therefore, the different laws were combined into two laws only: the Enterprise Law and the Investment Law.

#### *Adjustment Requirements for WTO accession*

Compared to other agreements such as the TRIPS Agreement, in the TRIMs case the drafting of legislation to prohibit local content schemes is

fairly simple and straightforward. In addition, there are no substantive technical requirements for compliance. However, phasing out all measures inconsistent with the TRIMs Agreement has proven to be difficult. The Vietnamese government has submitted an *Action Plan for the Implementation of the TRIMs Agreement*, which describes the changes of laws and measures already done and planned until 2007. The Action Plan demonstrates the government's commitment to phase out the local content and raw material programs by 2007 in order to comply with WTO law. The policies and measures mentioned above are not in conformity with the TRIMs Agreement and have to be phased out gradually.

Compliance with the TRIMs Agreement was a hotly debated issue for the Working Party on WTO accession. Some members of the Working Party criticized Vietnam for having introduced most TRIMs after the application for WTO membership, although "*acceding governments were expected not to implement new restrictive measures.*" (WTO 2006b, 85, para 329) Vietnam should "*comply fully with the TRIMs Agreement from the date of accession to the WTO without invoking a transition period.*" (Ibid.) This has been accepted by the Vietnamese delegation. Especially the preferential import tariff rates contingent upon localization ratios, which had been applied for a number of industries (motorbikes, cars, mechanical-electric-electronic industries have already been terminated (WTO 2006b, 71, para 275).

The case of incentives in the form of subsidies is less clear: TRIMs are typically used in combination with other policies. The question is how the phasing out of certain TRIMs, without regarding related policies, would affect trade. For example, local content policies are usually combined with a subsidy (Bora 2002, 174). The TRIMs Agreement restricts trade policy instruments but not the subsidy policies. However, the WTO Dispute Panel case on Indonesia has clarified that even incentive programmes (direct and indirect ones) are considered as TRIMs and, therefore, prohibited.

#### *What policy space will be left for Vietnam after WTO accession?*

The greatest challenge for industrial policy in Vietnam resulting from WTO accession and complying with the TRIMs Agreement will be to develop and technologically upgrade the ancillary industry so that foreign investors will buy more spares and inputs from local sources. This will be

even more demanding in future when import liberalization will make access to imported inputs even easier than today. Regarding the localisation ratios achieved during the last ten years, the motorbike sector has done quite well, while the automobile sector lags behind the targets for localisation. Thus, the government must find new measures for strengthening the ancillary industry.

Regarding the situation of FIEs, two trends can be expected: Foreign investment in import-substituting industries will decline with the lowering of import tariffs and other barriers. On the other hand, foreign investment into export industries may increase with easier access to imported inputs and with the expected rise in competitiveness of domestic ancillary industries from which foreign companies will buy their inputs without local content obligations, once these ancillary industries meet international levels of quality, reliability and costs.

#### 4.2.4 The case of the automobile industry in Vietnam

The development of Vietnam's automotive industry is ridden with the typical problems of a latecomer lagging about 30 years behind other countries in the region. The first modern car assembling plant, Mekong Auto, a joint venture of South Korean, Japanese and Vietnamese companies, was licensed in 1992. It was followed by no less than twelve foreign car manufacturers establishing assembly plants through joint ventures with Vietnamese investors. The rush of foreign car manufacturers to gain a foothold in the Vietnamese market must have been fuelled by excessive expectations about the growth of the market which have not materialized until today. Due to the low average per capita income, the market for cars in Vietnam is still relatively small. If today's optimal plant size for manufacturing passenger cars is around 200,000 units per year, Vietnam's 13 automobile joint ventures which have a combined annual capacity of only 173,000 units (according to the Vietnam Automobile Manufacturers Association, VAMA) rank far below international levels of optimal plant size. In 2002, only 27,000 cars were produced in Vietnam, whereas Thailand produced half a million cars, and South Korea more than 1 million cars, (*Saigon Times Weekly*, 24 May 2003). Since then, sales of domestically produced cars peaked with 43,600 units in 2003 (*Vietnam Economic Times* 122, 4 Jan. 2004). But even with this volume, the foreign and joint venture

car manufacturers in Vietnam used only a small fraction of their already relatively small combined production capacity.

Due to lower scale of production, cars assembled locally are far more expensive than the same or similar models on the international markets. Thus, car manufacturing is only viable in Vietnam as long as it is protected by high import tariffs and other measures. This protection was provided by a combination of high import duties and a special consumption tax, which was higher for imported than for locally assembled cars. But the high price level creates a vicious circle by restraining the demand for cars so that the industry cannot escape from the low volume trap. With this low volume split into 11 (today 13) plants producing a wide range of different models, it was impossible to create a sufficient demand for making a modern ancillary industry viable. Thus, the target for the localisation ratio of 25 per cent by 2005 as set by the Vietnamese industrial policy authorities could not be reached. If they want to meet the local content requirements imposed by the government, the foreign automobile companies cannot rely on an efficient local ancillary industry but have to produce their own spares and parts in-house which again is not cost-effective in comparison with international best practices of automotive industries.

#### *Legal requirements for automobile manufacturing and assembling projects*

The implementation of the *automobile components production program* is a condition for granting an investment license. This means in detail: The value of components and spare parts manufactured in Vietnam must account for at least five per cent of the finished automobile value no later than five years from the date of commencing production and must annually increase to reach at least 30 per cent of the automobile value at the tenth year of production (Circular No.215/UB-LXT 8/2/1995). One incentive for raising the local content ratio is the application of differential import tariffs on imported inputs and parts depending on the localization ratio achieved.



The application of different import tariffs according to the localisation ratio achieved will no longer be allowed under WTO law and will have to be phased out gradually.<sup>35</sup>

<b>Table 2: Incentive scheme for the production of automobile and motorcycle parts</b>				
Achieved localization ratio (in per cent)	MFN import tariff rates contingent upon localization ratios (in per cent)			
	With respect to parts which are subject to MFN import tariff rate of 30 %	With respect to parts which are subject to MFN import tariff rate of 40 %	With respect to parts which are subject to MFN import tariff rate of 50 %	With respect to parts which are subject to MFN import tariff rate of 50 %
1. Above 0 to 15	20	20	30	40
2. Above 15 to 30	15	15	20	20
3. Above 30 to 40	10	10	10	10
4. Above 40 to 50	5	5	5	5
5. Above 50	3	3	3	3

Source: WTO (2001a, 4)

In view of the low local content ratios reached so far, it seems that the Vietnamese government had expected too much from mandatory local content requirements for the foreign car manufacturers and did not invest enough effort in supporting the development of a competitive local ancil-

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35 Another incentive is a preferential corporate income tax for export manufacturing and processing projects using 30 per cent local raw materials (WTO 2001a, 6). But this is not relevant for the automotive industry which is producing only for the domestic market.

lary industry that would meet the quality requirements of the foreign assembly plants.

<b>Table 3: Average local content ratio in the automobile sector in 2004</b>	
Company	Local Content
All Foreign Joint Ventures together	2 %–10 %
Toyota	13 %
Trucks and Buses (below 24 seats)	10 %–20 %
Trucks with more than 24 seats	> 30 %
Source: Thanh (2004, 38)	

Only Toyota is aiming at a localization ratio of 20 per cent with the establishment of a new spare parts manufacturing plant (*Vietnam Economic Times*, 1 Jan. 2005).

<b>Box 6: Toyota's strategy towards SME suppliers</b>
<p>Toyota is open to any potential suppliers, regardless of nationality, size or whether this company is a first-time supplier or not. Toyota's co-operation with suppliers is solely based on business considerations, i. e. basically the economic and technological capacities of the supplier. Toyota expects its suppliers to excel in five key areas that characterise a competitive enterprise: quality, cost, delivery (regarding on-time delivery of the required quantities of inputs), engineering (including technology) and management. Since Toyota believes in developing mutually beneficial, long-term relationships with suppliers, trust and confidence as well as reliability are considered key factors. Finally, Toyota expects the enterprises to be able to continued improvement and enhancement of products, services and management.</p> <p>Toyota realised the importance of a local ancillary industry and wants to assist its suppliers. Therefore, often a preparatory process is needed for the suppliers before entering a business partnership with Toyota. Although Toyota has special programs to support SME suppliers, the support of the national government regarding policies and support measures for SMEs is decisive for overall success.</p>
Source: Muramatsu (2000, 1)

### *The Ministry of Industry's strategy until 2010*

According to the Ministry of Industry's strategy until 2010, Vietnam will focus on state-owned and large foreign companies to produce ancillaries (Thanh 2004, 37). A Vinamotor project aims at producing 50,000 auto parts per year by 2010, meeting a localization rate of 30 % by 2005 and 50 % by 2010. In October 2003, another project was approved to produce spare parts to meet 33 % of localization rate by 2005 and 50 % by 2010. This project, which is believed to cover market demand for popular cars in Vietnam, seems to be over-ambitious. However, projects focusing on assembling and manufacturing specialized vehicles such as trucks, vans and buses, and those focusing on manufacturing spare parts, will be facilitated and encouraged.

Recently, Vietnam's industrial policy toward the automotive sector has become somewhat contradictory. On the one hand, it still aims at developing a healthy automotive industry with increasing local content, on the other hand, there is the need to gradually liberalize imports and abandon differential treatment of domestically produced and imported cars in view of AFTA obligations and WTO accession, and, thirdly, there is a new problem coming up even on Vietnam's low level of development: Traffic congestion in the major cities requires action that may counteract the target of promoting the development of the automotive industry. The debate has started in Vietnam whether it will be necessary to cap the number of additional cars in the congested cities, and it may be taken as a justification, e. g. for maintaining the special consumption tax of 50 % (*Vietnam Economic Times*, 1 Jan. 2005). Under the trade liberalisation imperative, the Government of Vietnam has decided to allow from May 2006 the import of second-hand cars (up to five years old), however with an import tariff of 150 per cent, compared to the import tariff rate of 90 per cent for new cars. This will make it even more difficult for the existing car manufacturers to increase their sales and grow. Nevertheless, the government is reported to have licensed in 2005 two additional automobile projects, one for cars (Honda Civic) and one for trucks and buses (English.eastday.com, 20 March 2006).<sup>36</sup>

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36 One can only speculate whether the new foreign investors base their market projections on the estimation that the shadow economy in Vietnam may add 50 per cent to the official GDP (Tenev et al. 2003, 15).

*A development strategy for ancillary industries in conformity with WTO rules*

It is rather unlikely that Vietnam will be able to break out of the vicious circle of a low volume car industry by applying the traditional set of *national* industrial policy instruments. In view of the large scale of production that is needed for reaching international levels of cost competitiveness, the only realistic perspective is to encourage regional integration of automotive and ancillary industries in South East Asia. Trade liberalization within ASEAN and on the multilateral level under the WTO may pave the way towards deeper regional integration and specialisation of ancillary industries. However, overcoming the relatively fragmented structure of the auto industry in the region as a result of nationalistic industrial policies of the past era (cf. Ravenhill 2005) – which Vietnam has copied rather unsuccessfully – would require the combined will and coordinated action of the governments and industrial policy makers of the ASEAN and associated countries.<sup>37</sup>

With the necessary adjustments, Vietnam could become an attractive location for an automotive industry and ancillary industries linked to industries in other countries of the region. Automobile producers have started to investigate the possibility of out-sourcing the production of component parts to Vietnam, and whether it will be viable to produce for the world markets from there. To reach this goal, the regional trade for automobile components and finished cars must be further liberalised in the framework of AFTA and CEPT.

Vietnam does have comparative advantages in the region that make the country attractive for foreign investors in ancillary industries: It is a politically and economically stable country, not facing religious conflicts or strikes organised by trade unions. Its geographical location in South-East Asia and its long coastline make it easily accessible. Vietnamese are hard

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37 “So far, Vietnam has not taken an active role in ASEAN efforts to pool resources and enhance the region’s competitiveness. While a nationalistic tendency to create ‘complete’ industries in Vietnam is understandable given the nation’s hard-won struggle for independence, and may have fit well with the geopolitics of earlier times, it will only be through international integration and cooperation that economic development will progress rapidly in Vietnam, especially given the lack of modern industrial techniques currently in use.” (Sturgeon 1998, 16.)

working people eager to learn and to operate new technologies, which is very important in industries that face frequent changes of models, design, production patterns etc. Therefore, Vietnam should be well endowed for becoming a reliable partner for long-term relationships. Nevertheless, to build up an ancillary industry and increase its competitiveness, some reforms and efforts are needed:

- First, the Vietnamese government should provide coherent policies that are consistent with suppliers' demands, co-operate and interact closely in defining a development master plan, include upstream industries in their strategies, promote the development of human resources and of technological capacities and research and development (R&D).
- Second, to implement this plan successfully, the development of ancillary industries could be encouraged by general tax incentives (not related to trade performance). Provision of technical assistance for component and ancillary manufacturers should be encouraged through tax incentives. Industrial parks for clusters of component manufacturers should be established, where investors can profit from incentives for capacity building and from co-operating with each other in areas where similar tools and technologies are required.
- Third, to avoid overlapping investments, a close relationship and coordination between assemblers and component manufacturers is needed. The supporting industry should become specialised to produce large enough quantities so that they can benefit from economies of scale and increase their competitiveness (Duc 2004, 25).

Apart from these factors, foreign investors need transparent and reliable investment conditions. They are most concerned about the stability of policies and preferences. Laws should be clear and their changes should be minimised, and if any change is necessary, it should not be retroactive.

### 4.3 Enforcement of intellectual property rights

As a WTO member state, one of Vietnam's obligations will be to implement the rules of the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) within one year. Intellectual Property Rights (IPRs) are legal and institutional devices to protect creations of the mind

such as inventions, designs, and works of art and literature. They also include trademarks to distinguish a firm's product from similar ones sold by competitors (Dutfield 2003, 5). The economically most significant IPRs are patents, copyrights, and trademarks.

The purpose of this chapter is first, to assess the main challenges for Vietnam through the implementation of the requirements of the TRIPS Agreement. Second, the meaning of IPRs and of technology transfer for industrial development will be discussed. After a general introduction, the present situation in Vietnam will be analysed and conclusions drawn for Vietnam's future industrial and technology policy. The leading questions in this chapter are:

- What are the main challenges for Vietnam regarding the implementation and enforcement of the TRIPS Agreement? What remains to be done?
- What role do IPRs and technology transfer play regarding Vietnam's industrial development? Where should Vietnam focus on?

#### 4.3.1 The Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS)

According to the Ministry of Science and Technology, when the government filed its application to the WTO in 1995, Vietnam's "*industrial property system was far from compliance with the TRIPS Agreement. Generally speaking, the system was inadequate and ineffective.*" (MOST 2003, 13) This deficiency has three dimensions: the legal framework, the protection mechanisms, and the public awareness of IPRs in Vietnam. The following paragraphs assess the development and challenges regarding the implementation of IPRs legislation and the protection mechanisms available at present.

**Box 7: The TRIPS Agreement**

The TRIPS Agreement is the third pillar of the WTO alongside the agreements on goods (GATT) and services (GATS). It came into force in 1995. Since January 2000, all members of the WTO are obliged to comply with it. The TRIPS Agreement is to promote international harmonization of legislation on the protection of IPRs at a high level. Its aim is to improve the protection of IPRs, especially in the developing countries.

The agreement covers three aspects in particular: Firstly, it sets high standards for the protection of IPRs for the most important areas regarding industrial policy: patent rights, copyright protection, trademarks, geographical indications, industrial designs, layout-designs of circuits and undisclosed information. Secondly, the agreement contains detailed procedural guidelines that aim to ensure the enforcement of rights. Thirdly, if conflicts arise due to IPR infringements and non-compliance with the TRIPS Agreement, WTO member countries can submit the case to the WTO Dispute Settlement Procedure.

Therefore, the regulations of TRIPS go beyond all other existing conventions for the protection of IPRs, which are managed by the World Intellectual Property Organization (WIPO).

Although the implementation of the agreement is obligatory for all new WTO members since 2000, the agreement does not call for a complete international harmonization of protection. Therefore, countries retain a degree of flexibility in incorporating the agreement into their national law. Further room for manoeuvre exists because certain parts of the TRIPS Agreement are in need of and open to interpretation.

Source: WTO (2005a, 42); Liebig (2001a)

#### 4.3.1.1 Implementation of IPR legislation in Vietnam

Today, Vietnam's national legislation on IPRs seems to be close to compliance with the requirements of the TRIPS Agreement. An initial step for the Vietnamese government was the promulgation of the Civil Code in 1995, which contains a chapter on the protection of IPRs part (Part VI "Intellectual Property Rights and Technology Transfer"). Additionally, Vietnam signed the ASEAN Framework Agreement on Intellectual Property Co-operation in December 1995 and committed itself to the protection of internationally recognised IPRs (ASEAN Framework Agreement on Intellectual Property Cooperation 1995).

However, the most important milestone until today with regard to implementing IPR legislation was the signing of the US-Vietnam Bilateral Trade Agreement (US BTA) in 2001. Chapter two of this trade agreement contains obligations comparable to the WTO TRIPS Agreement: the US BTA refers to patent rights, copyright protection, trademarks, industrial designs, layout-designs of circuits and undisclosed information. In some areas the US BTA even goes beyond the TRIPS Agreement; for example according to Art. 5 encrypted program-carrying satellite signals are protected, an issue not mentioned under TRIPS. In comparison, additional provisions of the TRIPS agreement include MFN and geographic indications. As the implementation phase of the BTA rules ended in June 2004, the implication of the TRIPS Agreement for strengthening the protection of intellectual property rights in Vietnam will just be the final step towards full compliance with international legislation on IPR.

The current situation regarding the implementation of the required legislative provisions for IPRs can be assessed as follows: The last review of the Implementation of Vietnam's Action Plan, February 2004 (MOST 2004) demonstrates that Vietnam's national laws and circulars meet almost all TRIPS related areas, although in some areas only basically. Therefore, the action plan focuses on a variety of improvements to be made during the year 2004. According to the Review of the Implementation, the following measures are intended (MOST 2004, 11): Ensuring national treatment in establishing, maintaining and implementing IPRs; expanding the scope of protection of trademarks according to the TRIPS Agreement; providing implementing regulations on geographical indications; expanding the list of protected plants; providing concrete regulations on the establishment of IPRs regarding layout-designs (topographies) of integrated circuits and undisclosed information (Thang 2004, 9). Law experts state that, from the formal legal point of view, the laws and decrees on intellectual property rights are one of the best pieces of legislation in Vietnam.

Legislation on intellectual property has been streamlined in 2005 with the amended Civil Code of 2005 replacing the 1995 Civil Code, which entered into force on 1 January 2006, and with the new Intellectual Property Law of 29 November 2005, which came into effect on 1 July 2006. A number of decrees guiding the implementation of the new legislation were adopted in September 2006 (WTO 2006b, 95–96, para. 378). Of course, it will take some time before all state agencies involved and the courts will be fully



aware of and be able to implement and enforce the new legislation against infringements of intellectual property rights.

In addition to the efforts to bring Vietnamese national legislation in harmony with the TRIPS requirements, the government has initiated the process for signing and ratifying international treaties on important IPR issues. Since 2002 Vietnamese authorities have conducted studies for the participation in international conventions on IPRs such as: the Berne Convention on Copyright, the Geneva Convention on the Protection of Phonograms as well as the Brussels Convention relating to the Distribution of Programme-Carrying Signals Transmitted by Satellite (Thang 2004, 9). The accession to these conventions is planned for 2004.<sup>38</sup>

Regarding the implementation of IPR legislation and according to the opinion of several experts interviewed, chances are high that the legal requirements of the TRIPS Agreement will be fulfilled before Vietnam's scheduled WTO accession in 2006 (Nguyen / Toan 2003). At the moment, the main challenge for the Vietnamese government is to create more detailed legal devices for the different IPR issues and to provide implementation guidelines for the different laws and ordinances in order to fully comply with international standards and to provide assistance for the IPR holders and enforcement institutions.

In addition, the discussions between the National Office for Intellectual Property (NOIP), the Copyright Office and the Ministry of Justice regarding the attempts to separate the IPR legislation from the civil code demonstrate some remaining deficits in the area of legislation: according to statements of some of their staff, there exists a huge variety of different legal regulations<sup>39</sup> referring to the various TRIPS rules, sometimes even contradictory in their meanings. Separate laws for each IPR topic would provide a more transparent structure and would make the changing of provisions more flexible.

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38 Besides these steps the International Union for the Protection of New Varieties of Plants (UPOV) Secretariat has stated conformity of Vietnam's IP legal framework with the UPOV convention on new plant varieties after the incorporation of the UPOV's comments in the Vietnamese draft Ordinance on new plant varieties. Vietnam's accession to this convention is expected for 2004.

39 This refers to the mixture of laws, decrees and circulars: Circulars are decisions of the minister to stipulate the provisions of decrees. Decrees are promulgated through the government in contrast to laws which have to pass the National Assembly.

### 4.3.1.2 Mechanisms to protect IPRs in Vietnam

Part III of the TRIPS Agreement requires effective enforcement of IPRs through civil and criminal codes and administrative remedies and procedures, including border control measures. In addition, Part IV of the TRIPS Agreement stipulates simple and expeditious procedures for acquisition and maintenance of IPRs. Regarding the enforcement agencies, the agreement calls for timely, effective, fair and simple enforcement procedures.

The major challenge for Vietnam to comply with the TRIPS Agreement seems to be the remarkable divergence between the well developed legal framework and the frequent infringements of IPRs in Vietnam: One hears about business people copying products and designs and selling them under their own trademark or label. Recently, these problems have been contained to some extent. For example, in 2003 the Market Management Organization detected and handled 5805 cases of production and trading of counterfeit goods out of which one third was related to IPRs.<sup>40</sup> This, however, may be only the tip of the iceberg.

Compliance with the TRIPS Agreement was another hot issue during the sessions of the Working Party on Vietnam's WTO accession. Even the final report contains a number of very revealing questions and answers like the following: "*Some Members observed that it had been brought to their attention that some agencies of the Government of Viet Nam used computer software that had not be authorized by the right holder. (...) The representative of Viet Nam confirmed that prior to the date of accession, Viet Nam would issue appropriate legal instruments mandating that all government agencies use only legitimate computer software and not infringe the copyright of such software. (...) The Working Party took note of these commitments.*" (WTO 2006b, 101, para. 403)<sup>41</sup>

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40 The Market Management Office in Hanoi confiscated, e. g., thousands of fake articles of goods bearing "Nike" trademark of the Hanoi Textile Company.

41 "A Member urged Viet Nam to implement the TRIPS Agreement upon accession without recourse to a transitional period, stressing the importance of establishing appropriate laws and regulations, and adequate enforcement mechanisms. Some Members noted that although Viet Nam had implemented many intellectual property laws, Viet Nam also needed adequate enforcement mechanisms and sanctions to ensure protection of intellectual property rights, including civil procedures allowing plaintiffs to bring for-

The underlying hypothesis of this chapter is: On the one hand, there is a lack of awareness of and information about IPRs and their official protection among Vietnamese people. On the other hand, the enforcement is still too weak to solve Vietnam’s problems regarding the infringement of IPRs due to a lack of specific regulations, a lack of capacity regarding the registration area, a lack of co-ordination of the variety of enforcement institutions and a lack of knowledge among their staff.

The following box gives an overview about the structure of Vietnam’s enforcement institutions.

**Box 8: Institutions implementing and enforcing IPRs**

The Ministry of Justice is responsible for the legislation on IPRs in the Civil Code. Bodies working in the field of IPRs registration and protection in the broadest sense are the National Office for Intellectual Property (NOIP) under the Ministry of Science and Technology, responsible for trademarks, patents, copyright on scientific work and software; the Copyright Office under the Ministry of Culture and Information for copyright of literature and artistic works; the Plant Variety Office under the Ministry of Agriculture. These governmental institutions have the responsibility to assist their ministries in the management of IPRs but have no responsibilities to enforce IPRs directly. Recently, there has been a new struggle about responsibilities for different IPRs between the NOIP, the MOT and the Copyright Office regarding trademarks and the different copyrights. These struggles lead to an uncertainty among the business community and to permanent restructuring. Although this issue will not be discussed in detail here, the government should be aware that uncertainty is not a good base for domestic as well as foreign business development.

**Administrative procedures**

The power to enforce IPRs is given to various authorities, such as the People’s Committees at all levels, the Market Management Bureau, the Economic Police, the Inspectorate for Science and Technology and the Inspectorate for Culture and Information and the customs offices. The legislation gives these authorities sufficient power to deal with IPR infringements which are subject to administrative remedies. Without the authorization of the courts they can impose any appropriate statutory administrative measures within their competence. The sanctions range from admonition to fines between 5 and 100 Mio. VND. The law-breaker may also receive sanctions like revoking the business license, confisca-

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*ward actions regarding infringement, enforcement by the police, and border measures by the customs authorities.” (WTO 2006b, 118, para. 469)*

tion or destroying counterfeit goods, especially goods that may be harmful for human health or the environment (Nguyen / Toan 2003).

#### **Criminal Procedures**

As the production or distribution of counterfeit goods is a crime in Vietnam, there is the possibility for criminal procedures: the definition is that counterfeit goods are goods of inferior quality and utility; trademarks, industrial designs, indication of sources, appellation of origins and goods labels. Depending on the severity of crime, sentences can range from two years imprisonment to even capital punishment (Nguyen / Toan 2003). The application of death penalty for serious counterfeiting of trademarks has been criticised by some members of the Working Party on WTO accession as unacceptably severe (WTO 2006b, 117, para. 467).

#### **Customs**

In January 2002, Vietnam enacted the new Customs Law. The law provides that the clearance of imported and exported goods may be suspended in case the IPR owner submits evidence that his rights are infringed (e. g. through a certificate of trademark registration, primary evidence of the infringements involved etc.). The suspension shall not exceed the time limit of ten days or a maximum of 20 days (such time limits also conform to those set forth in the US BTA).

### 4.3.1.3 Challenges of IPR enforcement

As statements of interview partners show, Vietnam's SMEs are not well informed about the meaning of IPRs, and they do not have the capacity to bring newly invented products on the market and therefore feel forced to copy goods. In addition, there are more "professional" enterprises focusing on increasing their profits by using well-known brand names or trademarks without licences. What should be done to improve the situation in Vietnam? On the one hand, more information has to be disseminated about IPRs, the possibilities of registering own creations and the protection mechanisms, as well as about the possible punishment measures. On the other hand, nothing will change if the legislation protects all kinds of IPRs, but implementing regulations are missing and the enforcement bodies are weak. There is some similarity with China's problems of enforcing IPRs: *"In fact, IP rights are something foreign to Chinese culture. Confucian teachings encourage learning by copying, in stark contrast to contemporary principles of intellectual property rights. This philosophy resounds throughout Chinese culture. The ancient art of calligraphy is*

*taught by copying the style of great masters. It is not until a person has perfected the style of another that they are ready to develop their own unique style.”* (Gregory 2003, 324)

There are various ways to improve IPR enforcement in Vietnam. The first possibility to improve enforcement is through the implementation of specific regulations regarding enforcement remedies and procedures required by TRIPS. In February 2004, the government still assessed a lack of specific regulations on these remedies and procedures for the handling of infringement of IPRs as well as shortcomings within newly issued administrative procedures (MOST 2004, 13). The action plan for 2003/2004 therefore envisages perfecting the Civil Procedure Code and several other regulations. For example, it is planned to publish a circular guiding the proceedings of court cases concerning IPRs, to amend a government decree on the handling of violation of administrative regulations and to regulate the border control measures and procedures of handling IPR infringements in export and import activities. To guarantee compliance with the requirements of the TRIPS Agreement, Vietnam is on the right way to strengthen its efforts to implement the envisaged regulations.<sup>42</sup>

Secondly, the capacity for the registration of IPRs has to be improved. Referring to the necessary regulations for procedures for the acquisition of intellectual property rights (Part IV of the TRIPS Agreement), Vietnamese officials state their concern: Although the automation of administration of industrial property has been improved since 1996, it was not possible to significantly build up the capacity of the registration offices to ensure high-qualified procedures (MOST 2004, 16). For the future, NOIP plans to renovate the Organization and operation of the enforcement mechanism into a one-door system in which each body has its function (without overlapping of jurisdiction as today). A new idea is that one of the enforcement institutions would be designated as the co-ordinator to receive all com-

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42 E. g., in 1997/8 and 2001, even Sweden and Denmark were forced by the United States to bring their enforcement procedures in accordance with TRIPS requirements (see dispute settlement cases nos. 83 and 86 on the WTO website). The conflict cases were announced before the Dispute Settlement Body of the WTO but the different parties agreed on a mutually satisfactory solution: the defendants changed some civil proceedings to bring their national law in accordance to TRIPS. This might also happen so Vietnam, if the intended plans are not put into action.

plaints and co-ordinate the operations of the other bodies (MOST 2004, 17).

Thirdly, coordination and communication between the variety of enforcement institutions as well as the knowledge of the staff members need to be improved. In 1996, the Vietnamese government itself assessed the working of the institutions as cumbersome and bureaucratic, because the agencies had overlapping functions and their work was not well co-ordinated. According to several government officials and taking into account the voices of IPR holders in Vietnam, the situation has not yet notably improved, neither regarding the co-ordination among the different institutions, nor their level of knowledge and expertise.

The court system may serve as an example: the law agency Pham & Associates concludes that the lack of knowledge and the inexperience of judges often results in too long trials (normally, cases last up to three years) and that the court often does not take into account the rights holders' costs when calculating the damage. This prevents businessmen from bringing IP disputes to courts (Nguyen / Toan 2003). Foreign IPR owners seem to be more interested in effective measures to stop the infringement as soon as possible than taking an infringement case to the courts for compensation for the damage. While administrative measures seem to be more time- and cost-effective, infringements are more likely to be settled through administrative than through civil procedures. As long as there will not be a fundamental improvement in the handling of IPR infringements, foreign investors will be cautious to bring their latest technologies or inventions to Vietnam.

According to government officials interviewed there is still a lack of knowledge on IPRs even among the staff of enforcement institutions. This was debated even during the session of the Working Party, when the Vietnamese representatives had to concede that the general law enforcement agencies “*had no officials specialized in this area*”, and that “*no particular incentives were available to these officials to encourage investigation and prosecution of IPR infringements.*” (WTO 2006b, 113, para. 453) Training courses for ministry officials as well as for enterprises have taken place during the last years. However, these measures were not enough to educate all involved officials sufficiently on the relatively new issue of IPR. Reasons for that were the limited capacity of training measures and the reported theoretical bias and lack of practical orientation of the semi-

nars. This is one area where the Vietnamese government wants to concentrate its efforts because knowledge is the most important prerequisite for improvements for the whole enforcement system.

<p><b>Box 9: Action plan of the Ministry of Science and Technology</b></p> <p>Details of the action plan from 1996 according to TRIPS, Part III, enforcement agencies (still pending):</p> <ul style="list-style-type: none"> <li>– Establish separate courts responsible for industrial property/copyright matter in three to five regions.</li> <li>– Concentrate enforcement functions into two agencies (customs – border control; market control office – domestic market) and strengthening the capacity of enforcement agencies.</li> <li>– Strengthen the capacity (equipment, techniques, staff) for the enforcement agencies.</li> </ul> <p>Source: MOST (2004, 16)</p>
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Another issue is the reported informality problem within the enforcement institutions, especially regarding the handling of IPR violations. One interview partner of an intermediate institution said that if the certificate for the trademark or label for exporting goods is missing, one could easily solve the problem with extra payments. This is another major obstacle for effective protection of IPRs.

<p><b>Box 10: Enforcement of intellectual property rights in China</b></p> <p>The situation of enforcement of IPRs in Vietnam is often compared to the situation in China, however with a question mark: Although China is a WTO member since December 2001, the situation regarding IPRs shows still a lot of shortcomings. Many western industrialized countries complain about the widespread copyright infringements (music, software etc.) and product piracy. Therefore, the United States regularly threatens China through announcing the withdrawal of the WTO basic principle of guaranteeing most favoured nation treatment. But until today, no dispute settlement has been launched against China in this regard. As stated by representatives of the Organisation for Economic Co-operation and Development (OECD), the conditions in China have improved significantly during the last years: The legal framework as well as the needed institutions have been installed. However, especially in the provinces the administration lacks money and human resources. With activities like the realization of the “Intellectual Property Protection Publicity Week“ in April 2004, China challenges the infringers of IPRs.</p> <p>Source: Ermert (2004)</p>
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At present, the insufficient protection mechanisms are a growing concern among Vietnam's trading partners and foreign investors. It is obvious that this problem will be solved only in the long run. However, WTO membership will be an important step towards implementing the necessary reforms. In view of Vietnam's accession to the WTO, the widespread infringements in the area of copyright (music, software, designs) and counterfeit goods will not be the major obstacle – as long as Vietnamese enterprises do not export copied products on a large scale. Especially in the Asian region, but also in developing and even in developed countries all over the world, copyright infringements occur day by day. Until now, no WTO Dispute Settlement has focused yet on these issues directly, because the WTO law does not directly refer to individual citizens' behaviour, but only to government actions (or non-compliance).

But this does not mean that the effort to control the current infringements of copyrights for music or software should slow down. However, what is more essential is the fight against counterfeit products which are dangerous for the life of human beings or the environment, such as the copying of pharmaceuticals or spare part for automobiles and airplanes.

#### 4.3.2 Challenges for Vietnam's industrial policy

One important aspect of industrial policy is technology policy. Technology policy has two objectives: to support the development of new technologies and related know-how and to distribute the results among the business sector. According to a study carried out by the Central Institute for Economic Management (CIEM), a coherent government strategy for the development of a science and technology market<sup>43</sup> in Vietnam is missing. Urgent issues in that context are IPRs and investment in technological development by enterprises.

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43 A market of science and technology is considered to be a place where scientific and technological products and services are traded. Furthermore, it is regarded as an important channel in enabling enterprises to invest in technology renewal with a view to improving productivity and competitiveness of their products. In addition, a market for science and technology is considered to be a necessary environment for encouraging creativeness and innovation to improve national competitiveness (Dinh / Hong 2004, 65).



### 4.3.2.1 Influence of IPRs protection on industrial policy

During early stages of industrialization of the now developed countries, copying, imitation and adaptation greatly enhanced the diffusion of technology in industrialising countries. For example, the United States and Germany made use of British manufacturing innovations without paying compensation, and Japan borrowed extensively from US technological innovations (Lee 2002, 8). These possibilities are no longer available with the TRIPS Agreement and the effective Dispute Settlement Procedures under the WTO. In the area of patents, TRIPS provides a general level of protection for 20 years. Patent protection is available for semiconductors, computer chips and other technologies that are necessary inputs to industrial processes. Copyright laws include similar regulations for the protection of software and music, films and other artistic products.

A more effective enforcement of IPR legislation as required by the TRIPS Agreement will have ambivalent consequences for technological upgrading on Vietnam's industry. On the one hand, the practice of *reverse engineering* which had been quite common in Asian NICs (and in Europe at an earlier stage of industrial development) will be illegal. Companies will have to pay license fees for imported technologies. On the other hand, more effective protection of IPRs is expected to facilitate commercial technology transfer between foreign and local firms and from multinational companies to their subsidiaries in Vietnam. Foreign enterprises would feel more confident to apply latest technologies in the country without risking that everything new will be copied and used by local competitors (Bora et al. 2000, 22). In the long run, effective IPR protection would also create incentives for domestic firms to innovate and gain competitive advantages through new products and production methods. Since the WTO Agreement on Subsidies and Countervailing Measure (SCM) allows subsidies for research and development, and the results of this process can be patented, this would be the most effective form of industrial policy in compliance with WTO rules and agreement.

Generally speaking, developing countries do not have a comparative advantage for innovation. Therefore, to develop certain industrial sectors, they have to rely heavily on technology transfer from developed countries instead of relying on domestic innovation. With Article 66.2, the TRIPS Agreement urges developed countries to promote technology transfer to

least developed countries. But this has not had much real value due to the lack of absorptive capacity in these countries (Bora et al. 2000, 22). With more effective IPR protection however, the international allocation of R&D capacities might fundamentally change. During the last years, more and more international firms have established R&D centres, or have entered into collaboration agreements with existing R&D centres in China and in India. If Vietnam wants to participate in this “*profound shift of the center of gravity in the global economy*” (Ernst 2006, 29), it will have to strengthen its IPR enforcement system.

#### 4.3.2.2 State of the art of technology policy in Vietnam

As mentioned in the previous section, since the application to become a member of the WTO, Vietnam has made some ambitious steps regarding the issue of IPRs: Its national legislation on IPRs is at present almost compliant with the requirements of the TRIPS Agreement. Nevertheless a major gap between written law and practice can be observed. On the one hand, respect for IPRs is low and people have not developed the habit of registering IPRs. In 2002, only 743 patents had been issued in the whole country (out of 1,211 applications), and 132 licenses of intellectual property title transfer were certified in the relevant state management agency (Dinh / Hong 2004, 66). An ambivalent development can be assessed regarding the distribution between domestic and foreign registrations for IPRs in the period between 1990 and 2001. Although foreign invested companies still hold the majority in registering for granted patents for inventions, the situation becomes well balanced in the area of patents and trademarks. Vietnamese enterprises are one step ahead regarding granted patents for industrial designs compared to foreign enterprises (see Appendix: Tables 6–9).

But still, the overall number of registrations of IPRs by domestic enterprises is limited. In 2003, market transactions related to patents, useful innovations and model designs have been rare. There are various reasons for this situation: On the one hand, the existing management and policy mechanisms do not sufficiently encourage inventors of knowledge to register for intellectual property protection. On the other hand, protecting their intellectual property can be costly for enterprises and individuals (Dinh / Hong 2004, 69). In addition, many companies interviewed in vari-

ous industries (handicraft, textiles, shoes, furniture) claimed that registering a patent is not worth the trouble because the products are copied too quickly, even before the patent procedure is finalised. The complicated registration procedures take at least six months. In addition, the high costs, up to three million VND, prevent business people from registering their products or trademarks. Especially for SMEs, but also for large companies including SOEs, this situation means a loss of profit with regard to time and money spent on the innovation of a new product.

Regarding the area of trademarks, the Vietnamese business community seems to become more and more aware of the positive effects of registering one's own trademark, brand name or label for the selling on the domestic market and for exporting. But still, most of the Vietnamese goods are exported under foreign trademarks. Only recently, Vietnamese trademarks like *Trung Nguyen Coffee*, *PetroVietnam*, *Biti's Shoes*, *333 Beer* have been stolen by foreign enterprises (Outlook March 2004, 22).

A CIEM study demonstrates that the level of investment in new technologies made by Vietnamese enterprises is still very limited due to numerous reasons, related to the capacity of the enterprises on the one hand and to macro level policy on the other. The existing macroeconomic and business environment does not provide sufficient incentives for enterprises to invest in new technology. As long as there is no level playing field for different ownership types, subsidy mechanisms, existing privileges for selected enterprises, and uncertainties about policy changes, private entrepreneurs will be cautious to invest in R&D not knowing whether they will be able to reap the profits from successful inventions or technology improvements (Dinh / Hong 2004, 71). In addition to that, the private sector lacks capital, physical and human resources for investing in new technologies.

With the unclear perspectives for the future of state-owned enterprises, SOEs which still play a leading role in the economy, will not have an incentive in investing into R&D, regardless of IPR protection. SOE managers will rely more on government subsidies and protection against competition from the private sector and international competitors. The foreign enterprise sector has not been sufficiently mobilised due to the lack of an appropriate policy mechanism to induce multinational corporations to invest in technology-based manufacturing and service areas. In addition, absorbing and promoting technology transfer from ongoing foreign-funded projects in Vietnam has not been successful (Dinh / Hong 2004, 72).

Although the Vietnamese government has made some efforts to stimulate technology transfer, its strategy is criticized, especially by foreign companies (Norris 2003, 93–99). The regulation on the conditions of technological transfer (Decree No. 45) is strongly criticised for two reasons: on the one hand, a royalty rate, which may not exceed 5 % of the „*net selling price*“, is regarded as *unreasonably low*. On the other hand, the regulation that the IPRs owner loses his rights to the transferee after a seven year period is regarded as *being too short*.” (Norris 2003, 93)

In the twelve years from 1990 to 2002, only about 150 technology transfer agreements were approved by the Ministry of Science and Technology (MOST), among them an increasing number with subsidiaries of foreign companies. As the term “technology transfer” has been defined very vaguely (Norris 2003, 98), all contracts involving transfer of technology even for normal commercial licenses must be submitted for a review and approval by the MOST which can take years and may involve extensive interventions by consultants. At the moment, foreign entrepreneurs and international law experts feel that the current restrictions on technology transfer stifle Vietnam’s economic development and undermine its ability to develop its technology base.

#### 4.3.2.3 Conclusions for Vietnam’s future industrial policy

Firstly, Vietnam’s macro level institutions should continue their efforts to strengthen the legal implementation of international IPR legislation. In addition, the identified shortcomings regarding the enforcement institutions should be eliminated as soon as possible to guarantee effective procedures to register for IPRs and to prosecute infringements of IPRs.

To enhance technology renewal and investment in new technologies by enterprises, the government should continue its macroeconomic and structural reforms. Therefore, market economy institutions should be improved to create a level playing field for businesses. The consequence will be a more competitive environment that will force enterprises to upgrade technologies and invest in R&D. In addition, the government should continue to implement its policies of restructuring and equitizing SOEs (reducing subsidies and monopoly protection). Foreign investment should be encouraged to bring technology renewal and R&D activities to Vietnam and to collaborate with domestic science and technology research institutions

and domestic enterprises. In addition, the government should assist SMEs with financial and technical support for technology renewal in production (Dinh / Hong 2004, 73).

Secondly, the meso level institutions in the area of IPRs need more attention and support: At the moment, a wide variety of meso institutions is developing steadily in the area of IPRs, e. g. the Vietnamese Intellectual Property Association (VIPA) was founded in 2002 (see Box 11), and the Recording Industry Association of Vietnam was established in 2003. They already start to influence government policy as one interview partner of VIPA stated, e. g. through consultancy for new laws and regulations for the Ministry of Justice or the NOIP. Nevertheless there seems to be the need to strengthen their capacity to carry out measures of raising public awareness on IPRs and strengthen the representation of IPR holders' interests in front of the government. In addition, business associations like the Association for Garment-Textile-Embroidery-Knitting (AGTEK) or the Vietnam National Textile and Garment Corporation (VINATEX) should be strengthened to continue with their awareness building courses on IPRs protection as well as on programs regarding technological innovation and creative education (e. g. design courses).

Thirdly, the various business associations should provide more information on the meaning and relevance of intellectual property protection to their members, and try to influence government policies in this area. For example, although the importance to establish one's own trademark is widely known already, enterprises have to put more effort on this marketing possibility: Vietnamese companies should establish their own trademarks, brand names and labels in order to show their commitment to consistent high quality and to gain consumer confidence in the long run. Thereby, they could increase their sales and profits, first on the domestic market and in the future on export markets as well. For example, raw coffee gets just 38 cents per kg, but when the product is packaged and given a recognised brand name, it sells for US\$16 in North America (*Outlook*, March 2004, 22.).

**Box 11: The Vietnam Intellectual Property Association (VIPA)**

VIPA was established in May 2002. The non-governmental Organization aims at providing information about IPRs, especially for enterprises, Organizations and individuals working in the field of IPRs and to offer training courses on specific IPRs. In addition, the association has organised, in collaboration with the National University of Social Science and Humanity in Hanoi, a six months postgraduate course on IPRs. The pilot-course started in March 2004 with about 100 participants. However, due to the lack of staff members (currently only seven) and self-funding, the capacity of the Organization is very limited. The important advantage of VIPA is that due to the 700 actual members, the Organization has a creative pool of knowledge on IPRs from various points of views (lawyers, creators, enterprises).

Regarding the area of technology renewal, Vietnamese firms having a joint venture with a foreign partner should be more pro-active and build up the capacity to absorb the imported technology. In addition, the present weak link between private Vietnamese and foreign-invested enterprises, especially the supplier relationship, should gain more attention to be improved in order to profit from the possibility of better technological transfer (Dinh / Hong 2004, 72).

## **5 Challenges for export promotion**

Until recently, Vietnam's export success was based mainly on agricultural and mineral commodities, with some diversification taking place within the agricultural export sector. However, the high export growth rates of the past cannot be maintained by relying on agricultural exports alone. Vietnam has quickly gained major shares in world markets for agricultural commodities, and further expansion of the same exports may face diminishing returns. There will be a potential for higher value-added agricultural exports if Vietnamese producers and exporters will be able to produce constant high quality products and export them under premium brand names. But in the long run, further export expansion requires more diversification and will have to be based on manufactured exports. Like the earlier industrializing countries in the region, Vietnam will have to diversify its exports by exporting more sophisticated products with higher value added allowing for an increasing per capita income. Thus, diversifying manufactured exports and raising the value added of exported products

becomes increasingly important (Van Arkadie / Mallon 2003, 201). However, trade liberalization on its own will not lead automatically to a rise of competitive export enterprises and industries. Export-oriented manufacturing does not develop spontaneously with the availability of cheap labour and free trade. Active policies are necessary to support firms in their efforts to export new products to new markets (Rodrik 2004).

A common feature of industrial development in East Asian countries after the Second World War was that they did not stick to the traditional import substitution strategy for decades (as India, China and most Latin American countries had done). East Asian countries managed to combine some degree of import protection for new industries with an early drive to venture into exports. Their macro-economic policies did facilitate exports, but East Asian governments relied not only on sound macro-economic policies, they applied additional selective measures to encourage and facilitate early exports of new industries and even individual companies (e. g. through export contests). With this government-backed export orientation, East Asian countries encouraged their industries to adopt the latest technologies, management and marketing concepts in order to expand their shares in world markets and to finance the next round of industrial development from their own foreign exchange revenues. The WTO Agreement on Subsidies and Countervailing Measures, however, rules out the utilization of direct export subsidies, except for less developed countries, and Vietnam will not be exempted from the ban on export subsidies.<sup>44</sup>

The first section of this chapter examines Vietnam's export promotion policies in the light of WTO accession. Relevant export promotion instruments include subsidies, the services of Trade Promotion Organizations and policies to attract FDI (e. g. infrastructure development, human capital formation, establishment of export processing zones).

The second section deals with a special challenge for export promotion: the increasing relevance of technical regulations, standards and norms in

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44 *"Late industrializers may expect both discontinuity and continuity between GATT and WTO rules. The major difference between the two trade regimes from the viewpoint of late industrializers is the prohibition by the WTO of subsidies on exports. This prohibition terminates a very powerful developmental tool insofar as latecomers that made the transition from low technology into mid-technology industries after World War II made exporting, with subsidies, a condition for operating in protected domestic markets. Exporting was a performance standard that contributed to efficiency and growth."* (Amsden 2005, 229-30)

international trade makes it necessary to bring Vietnam's system of standardization in line with the international requirements and to provide Vietnamese producers and exporters with the necessary information and with the testing and certification facilities they need to meet the quality requirements of their export markets. Compliance with standards and norms on export markets is an essential precondition for exporting. Thus, helping exporting enterprises to fulfil these requirements can be regarded as an instrument of export promotion compatible with WTO rules.

### 5.1 Vietnam's export promotion policies in the light of WTO accession – *The challenge of competitiveness without subsidies*

What will Vietnam's accession to the WTO mean for its ability to promote industrial exports? What are the restrictions of promoting exports under WTO rules? What options remain and what can the Vietnamese government do? In the process of WTO accession and integration into the global economy, the Vietnamese government is confronted with two main tasks: It has to adapt its export promotion policies to WTO rules and it has to improve existing export promotion measures in order to facilitate the integration into the global economy. Thus, the purpose of this section is:

- to assess the WTO-compatibility of Vietnam's export promotion policies (especially industrial subsidies) and to identify required adjustments (section 5.1.1);
- to make recommendations on how to pursue an effective and WTO-consistent export promotion policy (section 5.1.2).



## 5.1.1 WTO-compatibility of Vietnam's export promotion policies and required adjustments

### 5.1.1.1 The WTO Agreement on Subsidies and Countervailing Measures (SCM)

The main WTO rules regarding export promotion are laid down in the WTO Agreement on Subsidies and Countervailing Measures (SCM). The SCM Agreement restricts the ability of WTO members to subsidise domestic production in a way and to a degree that would affect trade, i. e. it limits the scope for direct subsidisation of exporting firms. Subsidies are defined as financial contributions by the government or governmental agencies that provide a benefit to a specific enterprise, industry or region. There are different rules for three different categories of subsidies: Prohibited subsidies, actionable subsidies and permitted subsidies (Lee 2002, 6).

**Prohibited subsidies:** The SCM prohibits export subsidies for all countries with a per capita income above US\$ 1000. Furthermore, subsidies that encourage the use of domestic inputs rather than imported inputs are prohibited, as are subsidies that are conditional on export performance. Thus, setting export targets as a condition for subsidies is not allowed.

**Actionable subsidies:** In a grey area of subsidies, called “actionable”, subsidies are allowed in principle. However, if another member country can prove that it is negatively affected as a result of the subsidy, it can take action through the WTO dispute settlement process or by imposing countervailing duties.

**Permitted subsidies:** Three categories of subsidies are permitted: subsidies to disadvantaged regions, subsidies for research and development (R&D), and subsidies for environmental purposes. These subsidies represent possible loopholes for a limited range of export promotion measures. For example, international competitiveness of industries may be strengthened in conformity with the SCM Agreement through subsidising their R&D activities.

#### *Special and differential treatment on subsidies*

WTO law recognises that subsidies may play an important role in the economic development of developing countries. Therefore, low-income

countries with a per capita income of less than US\$ 1000 are exempted from the general prohibition of export subsidies. Once GDP per capita exceeds US\$ 1000, export subsidies must be eliminated within eight years after WTO accession.

Since Vietnam's current per capita income is below US\$ 1000, the general rule prohibiting subsidies would not apply. However, developing countries which have recently joined the WTO (e. g. China) were not able to negotiate special and differential treatment on subsidies even if their per capita income was below US\$ 1000. They accepted the obligation to rule out all existing export subsidies and not to introduce new ones in the future. The question whether Vietnam would be allowed to make use of the exemption clause allowing developing countries below US\$ 1000 to apply export subsidies was debated controversially among the members of the Working Party on Vietnam's WTO accession.<sup>45</sup> In the end, however, Vietnam accepted to eliminate all prohibited subsidies as of the date of accession, with the exception of incentives contingent upon export performance that were granted under current export promotion programmes. These incentives to current beneficiaries would be phased out over a five-year period beginning with the date of accession.

### *Incentives to attract FDI*

Concerning WTO law, there is a grey area with respect to the use of incentives to attract FDI. Competition between countries and even between provincial governments within one country for FDI is intense, and incenti-

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45 “Some members noted that Viet Nam considered itself a low-income developing country eligible to maintain export subsidies under the Agreement on Subsidies and Countervailing Measures (SCM). A Member expressed support for Viet Nam's inclusion under Annex VII of the Agreement on Subsidies and Countervailing Measures, owing to Viet Nam's low per capita GDP (less than US\$ 1,000). Another Member, however, noted that Article 27.2(a) of the Agreement was specific to developing countries referred to in Annex VII of the SCM, and this was not a self-nominated or expanding list of countries. Moreover, the provisions of Article 27.4 of the Agreement, available to developing countries with a small share of world export trade, would not be available to Viet Nam. While ready to consider some flexibility as to how Viet Nam would phase out its prohibited export subsidies, this Member maintained that Viet Nam should have no recourse to provisions allowing the use of prohibited subsidies following its accession. Moreover, as Viet Nam would be acceding to the WTO after the expiry of the phase-out period for export subsidies by developing countries, Viet Nam should phase out its export subsidy schemes upon accession.” (WTO 2006b, 72, para. 283)

ves are used widely by governments of developed and developing countries.<sup>46</sup> Most FDI incentives – such as tax incentives, duty exemption or duty drawback for exporting companies – fall under the definition of subsidies in the SCM. However, the concepts of the SCM Agreement were developed for subsidies affecting trade in goods and may not easily be applied to incentives for FDI (Bora et al. 2000, 21).

### 5.1.1.2 Consequences for Vietnam

For Vietnam, the concrete consequences of WTO rules on subsidies will depend on the outcome of the current negotiations in the WTO. Other WTO members of the Working Party on the accession of Vietnam have voiced concerns about the existing direct export subsidies. Therefore, Vietnam promised to phase out direct export payments contingent on export performance (*export rewards*) within five years of accession to the WTO and to scrap agricultural export subsidies immediately after WTO accession. However, Vietnam will maintain subsidies in the form of investment incentives for promoting development of new industries for another nine years.

**Prohibited subsidies:** At present, subsidies for manufactured exports are very limited in Vietnam. The government maintains only very few benefits conditional on exports that are not allowed under WTO rules. For example, the Export Reward Programme provides small benefits for successful exporters and is contingent on exports since the conditions for being rewarded require that enterprises have an increase in export value (CIEM 2004, 21). Hence, the government should be prepared to phase out the Export Reward Programme in accordance with WTO law.

**Actionable subsidies:** It is difficult to predict whether a conflict might arise in the middle category of “actionable subsidies”. Other WTO member countries have the right to ask for justification for this type of subsi-

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46 Multilateral disciplines on the use of incentives for attracting FDI would be in the interest of developing countries since this would level the international FDI playing field and prevent a waste of scarce resources when developing countries apply subsidies in competition for FDI. If Vietnam nevertheless intends to stimulate the development of a new industry through foreign investment, it would be a better policy to invest in attractive infrastructure, efficient institutions and a qualified workforce so that foreign investors consider the advantage of investing here over other locations.

dies and for evidence that they do not distort trade severely. This might be relevant for Vietnam's SOEs, which enjoy a number of production subsidies and preferential credits. Although these subsidies are not conditional on export performance, they could be regarded as trade distorting as soon as SOEs engage in exports. If another country can prove that it is negatively affected as a result of the subsidy, it can apply to the WTO dispute settlement or impose countervailing duties. This is not very likely to happen since the effect of *production* subsidies on trade is limited. However, production subsidies might pose a problem for SOEs producing textiles or garments. Thus, Vietnamese SOEs might face the charge of unfair competition if they receive any kind of state subsidy. Credit and tax preferences, debt rescheduling or debt cancellation for SOEs could be challenged by other WTO members.

### *Incentives to attract FDI*

Incentives for FIEs are certainly one of the most controversial issues. As mentioned above, it is not clear if incentives to attract foreign investment fall under the category of prohibited subsidies. Tax holidays and preferential tax rates – as currently applied to FIEs in Export Processing Zones<sup>47</sup> – as well as preferential credits, duty exemption or duty drawback for exporting companies may all be considered – in principle – as subsidies

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47 Export Processing Zones (EPZs) are not defined or referred to in WTO agreements. However, to the extent that trade-affecting subsidies are provided in an EPZ, the rules of the Agreement on Subsidies and Countervailing Measures apply. In general, restrictions on export subsidies under WTO law could limit the ability of countries to make use of EPZs in the future. Duty exemption, lower tax rates and special credit facilities could be contested by other countries because they represent subsidies to companies that are required to export a major share, if not all, of their output. However, there are other incentives to foreign investors that can be provided in EPZs, e. g. better infrastructure facilities and more flexible government regulations and services (taxation and customs procedures), which would still be allowed under the Subsidies Agreement of the WTO. In Vietnam, companies producing in and exporting from an EPZ enjoy tax breaks and different preferential tax rates, depending on their export orientation. It seems rather unlikely that Vietnam will have to phase out duty drawback schemes or incentives applied in Export Processing Zones (e. g. duty exemption, preferential tax rates). Although these incentives to attract FDI may not be fully consistent with WTO rules, they are still pursued by many countries all over the world. The Vietnamese government would do well to seek clarification on the compatibility of its EPZ policy with WTO rules and in this way avoid the possibility of future disputes with other countries. For an authoritative assessment of the economic rationale of EPZs and their compliance with WTO rules and agreements see: World Trade Report 2006 (WTO 2006a, 77).

prohibited under the SCM Agreement (Thang 2004, 8) . In the negotiations on Vietnam's WTO accession, WTO members requested to phase out all such measures that are contingent on exports. Vietnam is resisting, stating that such measures are necessary incentives to attract FDI and that they are consistent with the SCM Agreement (World Trade Organization (2000b).

### 5.1.2 Recommendations for an effective and WTO-consistent export promotion policy

Even if direct intervention by governments to support exports is increasingly restricted by WTO rules, this is not the end to an active export promotion policy. Subsidizing exports of uncompetitive products over a long time is a waste of resources and does not help to develop competitive export industries. More important than subsidizing uncompetitive products for exports would be the provision of an attractive investment environment for exporters. Instead of subsidizing exports, Vietnam should focus on reducing the still existing anti-export bias and on levelling the playing field between SOEs, private companies and foreign firms. Improving the overall economic environment should be accompanied by increased efforts to attract FDI. In order to strengthen export capacities of domestic companies, the government should encourage intermediary institutions such as Vietrade, VCCI and other business associations to provide all kinds of technical assistance (information on export markets etc.) to exporters.

#### 5.1.2.1 Reducing the anti-export bias and levelling the playing field for private and state-owned enterprises

##### *Reducing the anti-export bias*

Efforts to increase industrial exports will only be successful if the overall economic framework is favourable for exports. A stable macroeconomic environment is essential if export strategies are to succeed. Vietnam has an excellent track record of maintaining a stable macroeconomic environment since the start of the economic reform programme in the late 1980s. Combined with periodic downward adjustments of the nominal exchange rate by the Central Bank, this has helped to avert real exchange rate appreciation (Martin et al. 2002, 14). However, to facilitate integration into the

global economy, it is important to further reduce the still existing anti-export bias and to level the playing field between state-owned and private enterprises.

**Trade regime:** Despite considerable import liberalisation, Vietnam's trade regime remains biased against exports. High import protection still creates incentives to sell to the domestic market and reduces incentives to export. In addition to that, efficient exporting can be handicapped by quantitative restrictions on imported inputs, by higher than world market prices of imported inputs, and by the diversion of resources to the protected and capital-intensive industries.

**Duty drawback:** Well-functioning duty drawback systems are necessary until import tariffs are further reduced.<sup>48</sup> Interviewed enterprises stated that the functioning of duty drawback schemes has been improved in recent years. Procedures are faster and more transparent than they used to be. However, enterprises that export only part of their output are still facing problems. Administrative and bureaucratic obstacles remain an important barrier. For example, for calculating the inputs, which may be imported duty free, customs officers often take a long time for identifying the proportion exported out of the total output produced and the input-output ratios to be applied. There is obviously a need to shift from the current system of duty drawback, which is time-consuming and costly to an *automatic* system, which is based on pre-announced import-export ratios that could be applied for reimbursement of paid import duties. This would minimise corruption and reduce administrative delays (Lord 2002, 19). Encouraging exports through facilitating access to world-class inputs from abroad is good policy. However, Vietnamese economic policy makers should be aware of possible negative effects on domestic suppliers to exporting enterprises. If imported inputs are not taxed, whereas inputs from domestic suppliers are subjected to normal taxation, the latter are discriminated in favour of imported inputs. If Vietnam's small-scale industries are to become reliable and high quality suppliers to export oriented

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48 Protection of intermediate products handicaps export industries because it raises their costs to levels that are higher than those of their competitors in world markets. A possibility to offset this bias against exports is to allow exporting firms to import inputs and components at world prices through duty exemption or duty drawback.

foreign (and domestic) enterprises, they should enjoy the same tax rebates as imported inputs.<sup>49</sup>

**Regulatory framework:** Vietnam has gradually liberalised its customs procedures and import and export licensing requirements. Today, all domestic firms are allowed to export and import goods. Nevertheless, barriers exist that discourage trading by non-state enterprises (Auffret 2003, 5). Excessive regulatory requirements for private enterprises prevent them from exporting, and even export licenses are still required to export certain products such as steel, iron, motorbikes, automobiles, paper, fertiliser or chemicals and minerals. Vietnam's customs procedures are still too bureaucratic. For both exporting and importing a series of vouchers and certificates is often required, such as package proceeding documents, certificates of origin, export/import licenses for certain products or documents of the legal status of the exporting firm. In order to facilitate trade, these export and import procedures should be simplified and unified (Ministry of Industry 2003, 8).

#### *Levelling the playing field between private and state-owned enterprises*

The experience of other successful East Asian exporters shows that the domestic private sector has to be strong and dynamic if rapid export growth is to be sustained over a long period of time. In Vietnam, growth of the formal domestic private sector will depend on how quickly the government provides a level playing field between state-owned enterprises and private firms. The environment for private domestic investments has improved already. However, there is still discrimination between private and public companies with regard to bureaucratic formalities, importing/exporting possibilities, or access to capital and land (Dinh 2004, 21).

**Access to capital:** Discrimination between state-owned and private enterprises can clearly be seen in their access to capital. The banking system has to become more responsive to the needs of domestic private firms that often have difficulties in getting access to credit. For private enterprises, it

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49 "Another example of a misguided tax is the value added tax on domestic supplies sold to exporters. Since imports do not pay a VAT if they are used in exports, this virtually destroys the ability of Vietnamese firms to become local suppliers. But local suppliers lower costs and help encourage the rapid buildup of export clusters. Here again, the revenue gained is trivial, but the cost of lost activity is huge." (Dapice 2002, 15)

is also more difficult to borrow foreign currency than for SOEs. This is another barrier that hinders international trade activities of the private sector (Dinh 2004, 5). Vietnam has to create an independent banking system without government involvement in lending decisions. Instead of giving SOEs priority access to credit, state-owned banks should extend lending to private exporting firms. In addition, credits to private exporters should be further promoted through measures such as the export support credits of the Development Assistance Fund. These facilities help to compensate for the lack of a well-functioning financial system.

**Distribution of quotas for textile and garment exports:** Private companies also face disadvantages in comparison to SOEs concerning administrative procedures. A concrete example is the distribution of quotas for textile and garment exports to domestic companies. Private companies stated that it is difficult for them to get quotas and that they feel disadvantaged in comparison to SOEs. More transparent distribution procedures could ensure equal access to export quotas.

**SOE reform:** The reform of SOEs should be accelerated. Until today, SOEs, which are supposed to play a leading role in core sectors of the economy, enjoy significant state subsidies and protection. However, it remains unclear how these enterprises are to achieve competitiveness. While the protection might still be considered necessary to assist key industries of the economy, many other countries have experienced that the shorter the time, which is given to industries to adjust, the more likely the adjustment, will take place successfully.

**Reducing barriers to growth for private companies:** Private enterprises are already engaged in exporting, especially in handicraft, processed agricultural products as well as garments and leather products (CIEM 2004, 17). The export competitiveness of these firms can be further increased through larger production volumes and lower unit costs (*economies of scale*). To this end, existing barriers to growth for private companies have to be reduced. However, as long as the economic environment to invest and to do business remains in favour of SOEs, private enterprises face obstacles to grow and to become successful exporters. For example, in order to increase competitiveness through technological improvements and large production runs (*economies of scale*), private enterprises should be free to establish joint ventures with foreign partners. Private firms – with the involvement of foreign partners – have the potential to become export-



ers if equal opportunities are provided and existing barriers to growth (e. g. access to credit and land) are reduced.

### 5.1.2.2 Attracting FDI and strengthening export promotion through meso level institutions

#### *Attracting FDI*

Foreign companies already play a key role in increasing and diversifying Vietnam's industrial exports. The contribution of FDI to the expansion of manufactured exports has been significant. Since the entry of foreign investors is essential for further export success, the promotion of FDI has to be a cornerstone of any export strategy. This is not to deny the importance of promoting exports by domestic enterprises either directly or indirectly as ancillary suppliers to exporting foreign enterprises.<sup>50</sup> There are three tasks which are of special importance to make Vietnam more attractive for export-oriented FDI: Increasing consistency and predictability of economic policies, improving the country's export infrastructure and investing in human resource development.

**Increasing consistency and predictability of economic policies:** Foreign investors regard Vietnam's legal system and foreign investment policies as inconsistent and unstable and complain that policy changes can hardly be anticipated. For instance, they are concerned about changes in tax policies which reduce preferences enjoyed by enterprises in industrial and export processing zones and about the increase of the Value Added Tax applied to certain services provided for businesses in industrial and export processing zones.

Trust of foreign investors is hard to gain, but easy to lose. Thus, sudden policy changes regarding the framework for FDI should be avoided since they create uncertainties for FIEs. Companies cannot develop a long-term

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50 Having a number of well-known international firms in each export sector creates the special advantage of having a lobby inside the importing countries against unfair treatment of imports from Vietnam. The international networks of production and marketing that organize an increasing share of international trade are the best guarantee against major protectionist backlashes that would be a normal consequence of failed multilateral trade negotiations as could be the case with the presently suspended Doha Development Round in the WTO.

business strategy without stable government policies concerning, for instance, taxation, customs, licensing or land acquisition. Laws need to be clear and their changes should be minimised. If changes are necessary, they should be predictable, consistent and not retroactive. The application of legislation and regulations should be reliable.

**Export infrastructure:** A high-quality export infrastructure is necessary to increase export competitiveness and to attract more export oriented FDI. Although Vietnam has improved its infrastructure in recent years, the pace of improvement has not been as quick as in other countries in the region. As a result, many services have lower quality or higher prices. For example, electricity costs and fees for using seaport and airport facilities are higher than those of other countries in the region, as are water charges and fuel prices. Pricing policies for these utilities should be examined and, to the extent possible, revised to bring costs in line with those of other ASEAN countries (Lord 2002, 17; Dinh 2004, 21).

**Human resources:** Although the country's human resources are recognised to be comparatively well developed (compared to countries on the same per capita income level) and capable, they still fall short of the actual demands of investors. The shortage of high-skilled labour, such as managers or engineers is already becoming visible and might become even more severe in the future if the demand for high-skilled labour increases as a result of a stronger inflow of FDI (*Vietnam Economic News*, 13 April 2004). Besides providing universal primary education, more can be done to strengthen human resource development. The government should provide more technical training and relevant secondary and tertiary education to meet the growing human capital needs of exporting firms. In addition, incentives should be offered to encourage in-house-training (Perkins 2001, 485).

The exports of Vietnam could profit from the know-how and networking expertise of Vietnamese living abroad. Other developing countries with overseas diasporas have made considerable efforts and concessions to tap their resources and contacts in the countries of residence. The Taiwanese example has demonstrated how enterprises have benefited from migrants willing to return from the US to Taiwan. These individuals were former Taiwanese citizens who had studied or worked in the US, many of them in responsible positions in well-known companies. By using such a reservoir of human capital abroad, Taiwan was able to accelerate its industrialisa-

tion process. India is another country that has been increasingly successful in tapping the economic potential of its diaspora around the globe. On the one hand, they act as bridgeheads for Indian exporting companies in their countries of residence, on the other hand India has managed, through tax incentives and a steadily improving investment climate, to become attractive enough for Indian software experts and entrepreneurs to return from the US and other developed countries and invest their savings in new software enterprises in India which are well connected with international software networks and clients all over the world. Thus, India's success in becoming one of the leading software exporting nations is based on a far-sighted strategy to make use of its overseas diaspora.

While copying such an approach might be difficult for Vietnam, it is for sure a path, which would allow it to effectively profit from the benefits of the educational and technological know-how in the US and in other developed countries. Furthermore, it induces synergies by combining highly skilled labour from abroad with newly trained workers from domestic educational facilities. The appropriate educational and vocational institutions in Vietnam could then be upgraded more in line with the demands of the economy, thus making more efficient use of scarce national financial resources.

### *Export Promotion through meso level institutions*

Attracting FDI is one instrument for expanding and diversifying industrial exports, supporting *domestic* companies through export promotion activities is another. Trade liberalization alone will not automatically make export industries competitive. Domestic firms are often unable to seize the opportunities of new export markets without specific support. Thus, active policies are necessary to support enterprises in their efforts to export to new markets. In this context, institutions at the meso level – such as Trade Promotion Organizations (TPO) and Business Associations – play an important role in assisting exporters by reducing transaction and information costs and initiating learning processes. They can provide, e. g., information on conditions and requirements of foreign markets and services to foreign buyers.

Currently, a lot of changes and new activities are on the way to improve promotion of Vietnamese exports. Considerable progress has been made. New trading centres are being opened (e. g. the Vietnam Trade Centre in

New York) and new Internet services (e-commerce, match-making) have been introduced (CIEM 2004, 21). Recently, 143 national key programmes on trade promotion have been approved by the Prime Minister. These projects include organising international exhibitions in Vietnam and foreign countries, researching foreign markets, providing market information, human resource training and promoting national trademarks. Thus, Vietnam's trade promotion system is constantly improving. Nevertheless, to further increase effectiveness and efficiency, trade promotion institutions should focus on a variety of aspects:

- **Increased transparency of export promotion activities:** Export promotion activities are currently being planned or carried out by many different institutions. In addition to VCCI, Vietrade and Investment and Trade Promotion Center (ITPC), there are several business associations engaged in trade promotion activities as well as 47 provincial trade promotion centres (*Vietnam Economic News*, 2 April 2004). The first step to ensure the effectiveness of export promotion projects would be to make sure that information on these projects is made public. So far, accessible information on export promotion activities is limited and difficult to obtain. Information on export promotion activities could be pooled, e. g. in only one Internet portal. This site would give an overview of all ongoing export promotion programmes of the government and the different institutions engaged in trade promotion. The pooling of information would facilitate access to export promotion and ensure that export promotion services are equally accessible for all exporters. It would be particularly relevant for new companies that are starting export activities and searching for government support.
- **Language skills:** One problem concerning staff members of trade promotion Organizations as well as employees of exporting enterprises is insufficient command of English as the dominant language for international communication. For example, to make new business contacts with foreign buyers during trade fairs, good working knowledge of English is a necessary precondition. The impact of export promotion activities will be limited as long as this prerequisite is not met.

**Information on foreign markets:** As many Vietnamese enterprises stated during interviews, they are not yet able to seize the opportunities of new

export markets due to a lack of information on prices, quality standards and regulations on these markets. High information costs are an important export barrier, especially for newcomers to the world markets. Thus, one area on which Vietnam's export promotion should focus is the provision of market information, including forecasting of supply and demand, market surveys and information on quality requirements. Collection and dissemination of information on foreign markets have to be further improved. For example, market information provided by the commercial sections of Vietnamese embassies abroad seems to be of limited value due to lack of experience in collecting information and limited financial resources (Asian Development Bank 2003, 261).

**Match-making:** Information and transaction costs can also be reduced through lasting relationships between domestic companies and foreign buyers. Trade Promotion Organizations and business associations can play an important role in initiating contacts between Vietnamese suppliers and buyers from abroad ("match-making"). Foreign buyers provide necessary information on export markets and can assist domestic companies in improving the quality of export products (improving design, quality control, introducing new production technologies etc.). Thus, through long-term relationships with international buyers, a virtuous circle of growing exports, higher quality of products and improved competitiveness of domestic firms can emerge. However, some Vietnamese companies face problems in establishing longer-term commercial relations with buyers because the quality of their products is not consistent. Therefore, match-making activities could be supported by export promotion initiatives aiming at improving quality control.

- **Monitoring and evaluation:** In order to decide whether the different export promotion activities merit further efforts, projects should be carefully monitored and reviewed. Monitoring and evaluation is important to improve the accountability and transparency of projects, to learn from experience and to redefine strategies.
- **Meso-level institutions as mediators between government and enterprises:** Meso-level institutions have to perform two different tasks: On the one hand, they have to provide support, services and advice for exporting firms in order to reduce transaction and information costs for exporting. On the other hand, they should inform the government about the needs and concerns of exporting companies, influ-

ence government policies and act as mediators between enterprises and the government. So far, existing institutions can fulfil these two tasks only to a limited extent. Firstly, institutional support for exporting firms is still insufficient. The range of activities of export promotion organizations needs to be widened and their effectiveness and efficiency has to be improved. Secondly, the business community is only partially involved in the formulation and implementation of export promotion activities. Therefore, the government should aim at strengthening the dialogue with the business community, especially with private companies.

Summing up this section, one can conclude that WTO rules and agreements limit the scope for direct subsidization of exporting firms. Vietnam has agreed to phase out export subsidies upon WTO accession, so that the government can no longer direct industrial development through the use of (export) subsidies. Efforts to increase industrial exports will only be successful if the overall economic environment is favourable for exports. Internally, slow adjustment to changing global economic conditions, the lack of a dynamic private sector, and the inefficiency of state enterprises prevent Vietnam from improving its competitive position on major export markets (Lord 2002).

The first step to raise export competitiveness would be to “release the brakes” by removing all existing obstacles for (potential) exporters. This means to reduce the still existing anti-export bias, to accelerate the reform of SOEs and to level the playing field for all enterprises. Some private companies already have the potential to become successful exporters if equal opportunities would be provided and existing barriers to growth would be reduced. The second step to raise export competitiveness would be to formulate and implement an export strategy, which has to be based on two pillars: On the one hand, the investment climate for FIEs should be further improved to attract more export-oriented FDI. On the other hand, export promotion activities should be pushed to support domestic companies in their effort to become successful exporters.

## 5.2 Meeting the quality requirements of export markets – *The challenge of quality*

If export subsidies are ruled out by the WTO Agreement on Subsidies and Countervailing Measures – with few exceptions for least developed countries and for the transitional period in which major developed countries will have to phase out their agricultural export subsidies – Vietnam will have to focus its export policies and export promotion activities on improving the competitiveness of export products based on both cost advantages due to low labour costs in combination with increasing productivity and on consistent good quality.<sup>51</sup> There are already examples of Vietnamese export products, which are achieving higher prices on export markets through consistently higher quality. If this is possible for agricultural commodities like pepper<sup>52</sup> it will be even more relevant for manufactured goods for which quality aspects (design, functionality, reliability, safety etc.) play a greater role than for agricultural commodities. Vietnam seems to be in a good position to meet the quality requirements of export markets, and by aiming at high quality production for its exports it could distinguish itself from China’s “natural” comparative advantage in mass production of standardized goods.

The quality of products can be defined and assessed. There is a widening range of sophisticated yardsticks for prescribing and measuring the quality of products, especially in the developed world. “*We live in a world profoundly reliant on product standards.*” (WTO 2005b, 31) Standards for weight and length, specified properties and quality of goods have always been a fundamental precondition for market exchange. Industries develop standards so that complementary products fit together (camera and film, computer and software), and that division of labour and subcontracting within an industry is possible. Finally, quality conscious consumers demand reliable information about the properties of the goods they buy, and product standards are an objective instrument to provide a wide range of

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51 Even if Vietnam would not join the WTO, it will have to phase out its export subsidies. Other countries are becoming nervous with the large shares Vietnam has gained in relatively short time in the world markets for coffee, pepper and some other commodities. Vietnamese exports have already faced anti-dumping charges (e. g. the catfish case with the US), and other commodity producing countries would complain if they feel that Vietnam’s dramatic export successes are based on artificial pricing and export subsidies.

52 Cf. Clements-Hunt (2004).

information consumers need for making a rational choice, especially in view of avoiding health or environmental risks. They would not buy imported goods if they had no guarantee that these products comply with the same health and safety standards that have been introduced in their own country as a result of increasing public awareness of health risks and environmental degradation. Thus, technical regulations, standards and norms facilitate trade by providing both exporters and importers with reliable information about what they trade. On the other hand, standards can become a major trade barrier. Imported products that do not meet the mandatory standards (technical regulations) set by the government can be rejected. And even if the exporter meets the standards, there are costs involved in having the products tested and certified for compliance with the standards of the export market. With the general tariff reductions and dismantling of quantitative restrictions as a result of successful past, present and future rounds of multilateral trade negotiations, standards are becoming increasingly important in international trade.<sup>53</sup>

Vietnam's exporters will have to learn about and adjust to the standards and technical regulations of export markets, even if the country would not become a WTO member. Importing countries impose their standards on any product, domestic and imported from any source. The only difference WTO membership makes in the area of technical regulations and standards is that the WTO provides certain rules and special agreements for the application of standards in international trade. Vietnamese exports will be subjected to the same standards and to the same procedures for conformity assessment as imports from any other WTO member state (*most favoured nation* principle), and its exports will be subject to the same standards and technical regulations as domestic products of the importing country (*national treatment* principle). Of course, WTO membership implies the reciprocal commitment for Vietnam to respect the same principles when applying its own standards to imported goods and to implement the obligations of the relevant WTO agreements.

Finally, WTO membership will make it even more urgent to improve the quality of Vietnam's exports. Compliance with standards and norms on export markets is a precondition for making use of the improved market

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53 Consequently, the WTO has dedicated its World Trade Report 2005 to "Exploring the links between trade, standards and the WTO" (WTO 2005b).



access conditions that Vietnam expects from WTO membership. If Vietnam's exporters do not comply with the standards and norms of the importing country, their products will either be rejected by customs or they will not be accepted by companies which use them as inputs for processing, or by retailers demanding certain product qualities for their brands. In that case, Vietnam would experience only the negative repercussions of WTO membership (in terms of increasing import competition and a restricted policy space) without earning the benefits (in terms of export growth and diversification).

### 5.2.1 Increasing role of standards in international trade

With the general trend towards increasing product differentiation, standards providing information about the properties and qualities of products play an ever more important role in market economies. Minimum standards, or technical regulations (specifications), are set by legislation or government ordinances, these standards are *mandatory*, i. e., they have to be met by any product of the same category. Mandatory standards are, above all, regulations concerning dangerous substances. For example, in 1991 the German government introduced a ban of pentachlorophenol (PCP). PCP had been widely used as a preservative in wood products and in the leather industry. Immediately after that, products which did not meet the new very low ceiling on PCP content were rejected, e. g. leather jackets from India.

In many areas consumers demand higher quality and lower health and environmental risks. Industries and trading companies introduce *voluntary* standards for guaranteeing that their products meet certain criteria for safety, health or environment protection that are more stringent than the mandatory standards relevant for all products of the same category. Many consumers in Germany, e. g., feel a responsibility for environment protection and search for products with an eco-label. This gives industries a strong incentive to have their products tested for their environmental impact and to qualify for eco-labels. The information on voluntary standards is often given by a label that facilitates the search of consumers for products that meet their quality requirements. Labels as private standards have been accepted by the GATT and the WTO as a fact of life in international trade, because the consumers should be given whatever information they

need to decide which products to buy and whether to buy domestic or imported goods.<sup>54</sup> If a foreign firm producing in Vietnam for export markets is committed to such a voluntary standard, its Vietnamese suppliers have to comply with the same standard (Wiemann et al. 1998, 4; Wiemann et al. 1994, 5). Foreign buyers will give the companies from which they buy detailed prescriptions for the standards to comply with.

Another distinction between types of standards is especially relevant in international trade law: the distinction between *product* standards (e. g. ceilings on the content of hazardous chemicals or limits on the pollution of motor vehicles) and *production process* standards (e. g. emission controls, social standards like SA 8000 or ISO standards). Product standards are compatible with the GATT and WTO agreements, provided some preconditions are given: they have to be applied to domestic and imported goods alike (*national treatment*) and they have to be applied to all foreign products regardless of the country of origin (*most-favoured nation principle*). Process standards on the other hand, which specify the characteristics of a production process can generally not be imposed by the importing country on producers in the exporting country. If the importing country would prescribe to exporters in another country how to produce, this would violate the sovereignty of the exporting country. As long as the quality of the products is not affected, product inspection at the border does not provide information about the quality of the production process. If the importing country would require certain production process standards to be met by foreign exporters, it would have to send its own industry inspectors to the production plants of the exporting country. This is only justified in case of production processes which affect the quality of the traded products (e. g. hygiene standards for food processing or production of pharmaceuticals). The issue of process standards is highly contested in the international debate on trade liberalization and globalization. Environmentalists and trade unions in the developed world campaign against trade liberalization and globalization because they fear a *race to the bottom* in which producers in developing countries and countries with less stringent environmental

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54 In the 1991 dispute between United States and Mexico on US import prohibitions for Mexican tuna caught with nets which kill marine mammals (dolphins), the GATT Panel decided that the US import restrictions were not justified under Art. XX GATT, but it allowed labelling canned tuna products with a “dolphin safe” label in order to leave it to consumers to decide whether they choose higher priced products for the sake of environment protection (cf. GATT, 1991, 51).

and social standards enjoy a cost advantage over their competitors in countries with higher standards. Up to now the coalition of trading interests in the developed countries and governments of developing countries has been able to prevent the introduction of environmental and social standards, i. e. production process standards, into the WTO legal system. In fact, empirical studies have not shown that a race to the bottom takes place on a large scale, because other factors are even more relevant for international competitiveness of industries than environmental and social standards, e. g. productivity and reliability as a result of the technological capacity and infrastructure of a country, the availability of a skilled workforce, political stability etc.

In the era of globalization however, the distinction between product standards that can be enforced by importing countries and process standards that are not subject to foreign monitoring and intervention becomes increasingly blurred. There are too many concerns with global externalities, i. e. repercussions of production processes and standards in one country on the rest of the world. This is especially true for the impact of production processes on the environment (river and ocean pollution, climate change), for the risk of contagious diseases spreading around the world if certain hygiene standards are not met (e. g. avian flu), and even for the neglect of minimum social standards which might provoke social unrest and emigration of workers causing problems in the countries of immigration. Therefore, an increasing number of voluntary standards and labels requiring compliance with certain environmental and social standards in the production process have been developed in order to respond to the concerns of responsible consumers in the developed world. Since the monitoring of compliance is done by local NGOs or by buying agents and other representatives of importing companies, the governments of importing countries are not involved, and there is no conflict with WTO principles and agreements.

For a country like Vietnam aiming at higher quality exports, it will be advisable not only to comply with the product standards of export markets but also to improve the environmental and social standards of export production in both agriculture and industry. This would give Vietnam's exporters a competitive advantage over other countries with lower standards, especially when aiming at affluent consumers who often care most for

these issues and who are prepared and have the means to pay a higher price for products from “responsible sources”.

## 5.2.2 The role of GATT articles and WTO agreements

The principles for dealing with standards in international trade are contained in GATT Article III which says that imported products – after customs duties have been paid – may not be treated less favourably than the same domestic products (no other internal taxes or technical regulations can be applied that would discriminate imported against domestic goods). Thus, technical regulations and standards may not be used as a protectionist instrument in disguise. GATT Article XI rules out quantitative restrictions and import bans with the exception of import and export restrictions necessary for the implementation of standards. Finally, GATT Art. XX contains a number of exceptions to the general obligation to rule out quantitative import restrictions and other non-tariff barriers. Trade restrictions and other measures are allowed if necessary (among others) “*to protect public morals, to protect human, animal or plant life or health, for the protection of patents, trade marks and copyrights, and the prevention of deceptive practices, relating to the products of prison labour, and relating to the conservation of exhaustible natural resources*” (GATT, Art. XX).<sup>55</sup> These basic provisions of relevant GATT Articles have been spelled out in more detail in two agreements related to standards in international trade: The Agreement on Technical Barriers to Trade (TBT Agreement) and the Agreement of Sanitary and Phytosanitary Measures (SPS Agreement).

The TBT Agreement, which had been concluded during the Tokyo Round already, refers to “technical regulations” (mandatory standards imposed by governments and legislations), “standards” (guidelines for products or processes for which the compliance is not mandatory), and to “conformity assessments” (procedures by which the compliance of products with technical regulations or standards is tested and certified). In addition to the principle of non-discrimination and national treatment, the TBT Agreement urges members to apply relevant international standards as a basis for their technical regulations whenever possible. Therefore, members

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55 Thus, a reference to intellectual property protection, to social standards (prison labour) and to environmental protection (conservation of exhaustible natural resources) is already contained in the GATT.

should actively participate in international standardization processes and Organizations. In order to reduce the potential for conflicts over different national technical regulations, members are encouraged to accept equivalent regulations of other members when these fulfil the same objective as the own domestic regulations (the principle of *mutual recognition* of national technical regulations has been adopted by the EU in preparing for a fully liberalized market, the *Single European Market*). The TBT Agreement aims at increasing transparency in the area of technical standards by obliging members to inform others in advance on new regulations so that trade conflicts can be avoided, and to have all technical regulations published so that every exporter from another country can adjust his products to the regulations of the importing country. If an exporter would have to obtain conformity assessments in each of the countries to which he wants to export this would be a serious cost disadvantage in comparison to domestic producers. Therefore, the TBT Agreement obliges members to accept each other's conformity assessments provided they are based on the same procedures and carried out by reliable institutions. This encourages international accreditation of national testing laboratories and certification institutions.

The SPS Agreement which had been negotiated during the Uruguay Round and has become binding for all WTO members as part of the *single undertaking* of the Uruguay Round package of Agreements (the TBT Agreement which had been a plurilateral agreement until the end of the Uruguay Round, signed mainly by developed countries, has also become binding for all WTO members as part of the single undertaking) refers to the especially relevant issues of sanitary and phytosanitary measures applied for the protection of human, animal or plant life and health against pests, diseases and risks from additives, contaminants, toxins etc. in foods, beverages and animal feedstuffs. Since the emotionally highly charged issues of contaminated food causing diseases can easily be exploited by protectionist interests, the SPS Agreement requires that the measures have to be based on *scientific principles*; in case of conflict a protective measure can only be maintained if sufficient scientific evidence is provided that it is indispensable to achieve the objective of protecting human or animal health. This requirement however, can be overruled again in case of emergency or by inferring to the *precautionary principle* giving a member the right to apply a measure in anticipation of future scientific evidence for its

need (e. g. EU-US disputes over hormone beef and genetically modified organisms).

Thus, the WTO provides some protection against misuse of standards and norms for protectionist purposes. To give a hypothetical example: in case the Vietnamese government could provide evidence that the EU had imposed a new environmental or health standard only with the aim of keeping certain products originating from Vietnam off the EU markets, it could take even the EU “to court”, i. e. to the WTO Dispute Settlement Procedure. The EU would then have to prove scientifically that the measure is necessary for protecting European consumers.

### 5.2.3 Vietnam’s institutional capacity in the field of standards and technical regulations

Vietnam has a relatively elaborate system of standards and technical regulations. Standardization began in 1962 already with the establishment of the Institute for Standardization and Metrology in North Vietnam. The first Vietnam Standards (TCVN) were developed and published in 1963 – today there are more than 5600 TCVNs. The Vietnamese standard system had been developed in the central planning era, and is now in transition to a more flexible system geared to the needs of an open market economy. In the old days, *“Vietnam’s standards were based on Soviet norms, which were typically mandatory but largely ignored (...). The move towards non-mandatory standards and technical regulations, and shifting much of the quality responsibility away from the government, is part of the ‘second stage’ of transition for economies like Vietnam, China, Russia and the Ukraine.”* (McCarty 2000, 16) This has two aspects: First, Vietnamese standards have to be based more on the relevant international standards; this is imperative both in view of WTO membership and for facilitating access of Vietnamese products to Western export markets. Second, the standardization system has to change its role from a government system operating with decrees and direct steering of state-owned industries to a market economy in which standards are developed in close cooperation between government and private business.

On paper and Internet websites, Vietnam’s system looks well organised with all functions covered by specialised institutions. Nevertheless, there seems to be a lack of capacity for covering the needs of a fast developing

and opening economy in which the private business sector has to learn the importance of technical regulations, standards and labels, especially in international trade, and in which the government standard institutes must change their attitude from a top-down approach to a more cooperative and service oriented interaction with the business community.

The top government body for standardization policy is the Directorate for Standards and Quality (STAMEQ) under the Ministry of Science and Technology (MOST). STAMEQ prepares the rules and regulations on standardization, establishes the organizational system for standard setting and implementation, for quality control and quality management, conducts studies and provides training in the field of standardization. These activities are based on Vietnam's 1991 Act on Product Quality. The concrete development of Vietnamese standards (TCVN) is the task of the Vietnam Standard Centre (VSC), which is a branch of STAMEQ. The VSC organises the various technical committees and subcommittees that are preparing new or reforming existing the standards. There are two technical institutions under STAMEQ for conformity assessment (testing) and certification of products that meet the required standards: QUATEST and QUACERT. Finally, the Bureau of Accreditation under STAMEQ operates various accreditation schemes for laboratories, certification and inspection bodies.

To increase transparency of technical regulations and SPS measures, WTO members are required to establish TBT and SPS Offices as enquiry points (Wilson 2002, 434). In view of WTO accession, Vietnam has established a National Enquiry Point on technical barriers to trade ([www.tbvtvn.org](http://www.tbvtvn.org)) through which trading partners can obtain information on Vietnam's standards and technical regulations and on the standardization system. The Enquiry Point operated by STAMEQ offers information in both directions: domestic parties can also contact it for information on TBT issues of other WTO members. The Enquiry Point will function as a notification point in the sense of the TBT Agreement only after WTO accession. In the meetings of the Working Party on Vietnam's accession to the WTO, "*the representative of Viet Nam confirmed that Viet Nam would comply with all the obligations under the TBT Agreement from the date of accession without recourse to any transitional period.*" (WTO 2006b, 78, para. 303) It was also confirmed that Vietnam "*would comply with the requirements of the SPS Agreement upon accession without recourse to any transitional*

*arrangements.*” (Ibid, 84, para. 327) Vietnam (STAMEQ) is member of the major international and regional standardization Organizations, ISO, CODEX Alimentarius, ASEAN Consultative Committee for Standards and Quality etc.

Although the Vietnamese system for standardization, conformity assessment and accreditation looks well organised with the different functions given to different bodies, there are doubts about its effectiveness and its preparedness for the new challenges of WTO membership and international competition. In 2006, the debate in the National Assembly about a new law on standards and technical specifications brought to the fore some shortcomings of Vietnam’s standards in view of what will be required from a WTO member state. According to the Chairman of the National Assembly’s Committee for Science, Technology and Environment, “standardization activities in Vietnam are backward and ineffective.” Only 24 % of Vietnam’s standards are in line with international standards (*Vietnam Net Bridge* 24 Feb. 2006). It is hoped that the new law on standardization (which will come into effect in 2007) will make the system more efficient and thereby raise the competitiveness of the economy and help to expand exports and attract foreign investment. Similar to the problem with intellectual property rights, the major problem in the area of standardization may not be legislation but effective implementation and enforcement. The national testing and certification infrastructure does not yet meet the needs of Vietnam’s expanding and diversifying export business.

Conformity tests are necessary to prove that a product meets the quality criteria set by either a technical regulation or a voluntary standard. Depending on which properties of a product have to be tested, more or less sophisticated laboratory equipment is needed. This equipment can be extremely costly, and it has to be operated by highly skilled staff in order to make the tests reliable and compliant with international standards for testing. Developing countries face severe problems in complying with the standards of their export markets because they do not have the testing laboratories needed for an ever wider range of criteria demanded by the importing developed countries. In that case, the conformity assessment can be done only by international testing laboratories or by laboratories in the importing country. This raises the costs and involves the risk of products being rejected for non-conformity after shipment.



Although Vietnam does have a diversified institutional infrastructure for inspection, testing and certification of (export) products, there are still some shortcomings. A number of firms interviewed reported that they had to send export products for testing abroad, to Germany or Taiwan. For some chemicals there are no laboratories with the specific machines, which are very expensive. For example, wood processing and some properties of seafood cannot be tested in Vietnam. Another problem seems to be a lack of confidence in the quality of inspection services because of *“fierce competition between inspection activities in the market (...). As a result, there is an urgent need for a mechanism to bring back the confidence in these activities.”* (APLAC News Notes No. 076, October 2004, 5) If foreign buyers do not have confidence in the testing and certification of Vietnamese institutions, they will prefer to do their own testing. They will send their representatives to the supplier’s factory to do inspection on the spot and avoid the risk of rejection after shipment. Smaller buyers, who cannot send their own inspection staff, will rely on the services of foreign firms like TÜV Rheinland (Germany) or SGS (Switzerland) which offer pre-shipment inspection, testing and certification.

Testing alone is necessary but not sufficient for gaining access to foreign markets and confidence with buyers and consumers abroad. The customers must have confidence in the quality of the tests and the reliability of the certificates issued by the testing agency. Certification institutions often have commercial interests and may be interested in selling as many certificates as possible. Thus, there is a conflict between *“selling certificates”* and *“ensuring quality”*. This conflict can be solved by independent accreditation institutions. The quality and reliability of a testing laboratory/agency can be certified by having it accredited with an impartial Organization in which the customers trust. Of course, they will trust most in their national accreditation Organizations and in international ones. The task of an accreditation institution can be described as *“certifying the certification institution”*.

In order to ensure reliability, the accreditation institution has to be independent from the certification institution. In Vietnam, there seems to be a problem with the institutional independence of testing and accreditation institutions. The institution responsible for accreditation is the Bureau of Accreditation, which belongs to STAMEQ. Therefore, it may be questioned whether it is independent enough from the certification institutes to

accredit them a reliable way.<sup>56</sup> What is even more relevant, there seems to be a lack of international recognition of the accreditation STAMEQ gives to domestic laboratories.<sup>57</sup>

#### 5.2.4 Quality consciousness of the business community

Even though some industries in Vietnam have already reached high quality levels, there seems to be a lack of awareness of the importance of meeting the quality requirements of export markets. Companies with own export activities or frequent contacts with foreign buyers are quite aware of these requirements, others less. Companies that want to venture into export production should be given early information and training about the technical regulations, quality standards, eco labels etc. that are relevant for their export business in the target markets.

Visiting industrial areas and individual companies in Vietnam, one gets the impression of an inflation of ISO-Standards like ISO 9000 or ISO 14000<sup>58</sup> among Vietnamese companies. A few enterprises also have SA 8000.<sup>59</sup> Thus, it seems to become fashionable and part of marketing strategies to show the quality commitment through these labels. However, these standards indicate the quality of management and of respecting environmental standards in the production process. They are *production process* standards and not *product* standards. Thus, they may be regarded by overseas customers as a first indicator for a reliable supplier, but they do not provide information about the quality and reliability of the products. Com-

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56 The problem of the lack of separation of the policy-making role of STAMEQ from its functions of certification and accreditation was discussed in the Working Party on Vietnam's accession to the WTO (WTO 2006b, 74, para. 290).

57 According to a 2003 joint document of the Ministry of Science and Technology and UNIDO, "*no laboratory in Vietnam is as yet accredited by an international body.*" (MOST / UNIDO 2003, 18.)

58 ISO 9000 is primarily concerned with "quality management". It refers to customer's quality requirements and applicable regulatory requirements for example. ISO 14000 is primarily concerned with "environmental management". It refers to the minimization of harmful effects on the environment for example (see International Organization for Standardization: <http://www.iso.ch/iso/en/ISOOnline.frontpage> (assessed: 14 April 2004)).

59 SA8000 is a social standard. It is based on international workplace norms in the International Labour Organization (ILO) and the UN's Universal Declaration of Human Rights and the Convention on Rights of the Child (see Social Accountability International; online: <http://www.cepaa.org/SA8000/SA8000.htm> (assessed: 14 May 2004))

panies having these general quality management labels face the same market entry barriers as others if their export products do not comply with the relevant technical regulations of the importing country.

For European buyers in particular, ISO 9000 would be only a first indicator of the commitment of a company to quality management. The more ISO 9000 labels one sees at every company entrance, the more suspicious buyers may become of the real meaning of this label, especially if one hears about fierce competition among certification agencies. European buyers will prefer to visit the companies themselves to assess with their own criteria whether they are committed to quality management. What is really important is the quality of the *final* product. It is important that it meets the mandatory standards in Europe and, on top of that, the voluntary standards of certain quality or environmental labels and of individual buyers, like German departmental stores and mail order houses.

By providing assistance to enterprises, foreign buyers can raise awareness and encourage implementation of standards by their suppliers in Vietnam. Thus, exports can be promoted through inviting more buyers from Europe and other developed regions to put up their buying offices in Vietnam. They have a commercial interest to find reliable suppliers with whom they share their market information and whom they may even give technical assistance for meeting the quality standards of their home market. More and more Vietnamese products show up in departmental stores and furniture store chains in Europe, indicating that it is possible in Vietnam to manufacture the quality required on European markets. Foreign enterprises manufacturing in Vietnam for export markets are another source of information on technical regulations and standards to be met by their local suppliers. Some of them provide written information on quality requirements to their suppliers. Furthermore, many of them have detailed talks with their future suppliers before starting the co-operation and they work out corrective action plans in co-operation with them. Some foreign enterprises send their Vietnamese employees to training abroad, so that they gain a better awareness of the standards and quality needed for satisfying the customers.

Besides the direct business channels, information on technical regulations and standards relevant for export production and marketing is offered by a number of institutions like, for example, the Vietnam Chamber of Commerce and Industry (VCCI), the Investment and Trade Promotion Centre

of the People's Committee of HCM City (ITPC) and the Vietnam Directorate for Standards and Quality (STAMEQ). Furthermore, there are also various Vietnamese business associations providing information and technical assistance. Apart from the Vietnamese institutions in this area, there are foreign agencies offering all types of information on European markets, like the Centre for the Promotion of Imports from Developing Countries (CBI) (Netherlands)<sup>60</sup> and foreign Chambers of Commerce like the European Chamber of Commerce in Vietnam.

Vietnamese exporters should regard the challenge of high standards on export markets as an opportunity to demonstrate high and consistent quality of their products. Quality of products, and higher environmental and social standards of production processes could become a competitive advantage of Vietnam in comparison with, e. g., China. In these areas Vietnam on the whole seems to perform better than other countries in the region. Some industries, like garment and furniture, are already characterised by the high quality of their products, but others have not yet reached this high level.<sup>61</sup>

The Vietnamese government should focus its industrial policy activities on providing the best services possible for stimulating and supporting a strategy of quality exports of Vietnamese industries. To conclude, one can say that by improving awareness of *product* standards, by building up more testing and certification agencies and by improving reliability of the accreditation institution, Vietnamese enterprises will have better opportunities to succeed in exporting to the developed countries, especially in Europe.

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60 The Dutch trade promotion agency CBI in particular provides a lot of information and assistance concerning the compliance with international standards and standards on export markets. One can get a short overview on its web-page [www.cbi.nl](http://www.cbi.nl).

61 *“There have been cases where access to export markets was denied due to sanitary or phytosanitary issues, resulting in substantial costs in terms of lost sales and market share. But rising standards also serve to accentuate underlying supply chain strengths and weaknesses and thus impact differently on the competitive position of individual countries. Some countries are able to use high quality and safety standards to reposition themselves in global markets.”* (WTO 2005b, 160)

## 6 Conclusions on Vietnam's industrial policy and recommendations for trade-related development cooperation

### 6.1 Adapting industrial policy to the WTO framework

It has been shown that there is a need to reform industrial policy according to WTO provisions. Reforming industrial policy instruments is of special importance since there will probably be little room for exemptions (*special & differential treatment*), only longer transition periods might be negotiable. To comply with WTO rules, the most important prerequisite for industrial policy instruments is to avoid trade distortions. Trading partners can apply to the WTO Dispute Settlement Procedure if trade is negatively affected by policy instruments of other countries. Furthermore, equal treatment (ownership neutrality) regarding private, state-owned and foreign invested enterprises has to be implemented as a basic principle of policy-making. Therefore, *generic* policy instruments instead of specific interventions should be pursued. In the concluding remarks, the direction and challenges of an industrial policy shift in Vietnam are summed up briefly for the macro level, the meso level and the business sector.

#### 6.1.1 Macro level: How to provide a level playing field?

On the macro level, providing a level playing field for private, state-owned and foreign invested enterprises will probably be the most important task. Therefore, it is advisable for the Vietnamese government to complete the paradigm shift from activist and specific industrial policy to neutral and incentive based policies. As shown in the study, the necessity of a change in policy instruments is most obvious in the case of import liberalisation and localisation policy. Regarding the latter, the traditional policy tool of local content requirements that has to be removed according to WTO law could be replaced by incentives for establishing and improving domestic ancillary industries so that they become attractive for domestic sourcing of foreign investors. Regarding trade liberalisation, tariff reductions required for WTO accession will force the Vietnamese government to make use of other incentive measures than selective protection to support industrial development. Therefore, it is advisable to focus on sustaining and building up a sound macroeconomic framework, an attractive investment climate

and a level playing field for all economic actors. According to the findings of this study, the most important ingredients for a paradigm shift in industry policy would be the following:

- *Providing an efficient infrastructure* is a challenging task for the Vietnamese government: First of all, physical infrastructure like roads, railways and ports need to be improved. Second, improvement of trade-related services through privatisation and opening for foreign investors can have the same positive effect on efficiency of exporting as the physical infrastructure. So far, private and foreign enterprises have limited access to banking services and financial sources due to either specific regulations or differential treatment of private vis-à-vis state-owned enterprises. Opening the financial sector to private and foreign investors will have to be complemented by a *modern banking regulation and supervisory system* that stimulates competition and avoids the spread of financial crises through irresponsible lending. An efficient physical and services infrastructure is an important precondition for Vietnam to attract more FDI that will play a key role for developing and diversifying Vietnamese exports. And, finally, Vietnamese exporters also need an efficient infrastructure for product testing and certification, which is already working well in Vietnam but still leaves room for improvement in terms of quantity and quality.
- *Human resource development* is a second challenge. There is an increasing shortage of high skilled labour. Vietnam already has a good basic education system that should be maintained and improved, too. On the one hand, human resource development will be a prerequisite for attracting more technologically advanced FDI to Vietnam. Government support for human resource development is also a prerequisite for enabling domestic ancillary industries and exporting firms to absorb modern technologies and production concepts so that they become reliable partners for international firms both in Vietnam and outside.
- *Supporting research and development (R&D)* within companies, universities and research Organizations is a third instrument of industrial policy that is in conformity with WTO rules and agreements. Research and development is not yet a common practice of competition among Vietnamese enterprises. Since this is a precondition for competing in international markets and adapting to changes in demand

and product development, the government should support R&D activities together with technology transfer to the business sector. Government assistance to R&D and to improving technological capacities of domestic industries is an indirect instrument to improve the quality and competitiveness of exports. And it would make Vietnam a more attractive location for export oriented FDI that are searching for local suppliers of high quality inputs. Close cooperation between foreign companies and local ancillary industries manufacturing according to the technological and to quality requirements of the foreign firms is another stimulus for permanent technological upgrading of Vietnam's industry that works even without strong local content requirements. To support engagement in technology development and renewal, the protection of IPRs and registration facilities have to be strengthened.

- Vietnam already has a sound record of economic and political stability. However, the government has to prepare itself for policy changes as a consequence of economic liberalisation and the commitment to global integration. For example, *more transparent policy making processes and a reliable decision making process* are two elements that need to be improved in the near future. This is of particular importance for attracting more foreign investors and for promoting exports in the future. For example, the distribution of garment export quotas to EU markets is said to be intransparent thus restricting competitive enterprises from further trade profits. However, it became clear during the interviews that reliability does not only depend on the political and juridical process, but also on *efficient and transparent administrative and juridical implementation procedures*. This is particularly relevant for the enforcement of IPRs where a large gap between law and practice prevails. Exporting modern manufactured goods requires easy and timely access to imported inputs. Therefore, improvement of administrative procedures at the customs offices is especially important for exporting firms. In both fields, delays and cumbersome procedures prevent the private business sector from gaining competitiveness on international markets.

In brief, many of the efforts that have to be made with regard to WTO accession, focus on the development of a modern industrial policy that prepares and supports the country and its businesses for global integration.

## 6.1.2 Meso level: How to influence government policies?

According to the interviews, meso level institutions like the Vietnamese Chamber of Commerce and Industry (VCCI), the Hanoi Union Associations of Industry and Commerce (HUAIC) or the Vietnamese Intellectual Property Association (VIPA) already act as intermediate institutions between the business sector and the government level. Business associations already channel proposals for improvement from member companies to decision makers in the government. In addition, some institutions act as consultants in the development of new legislations. This concerns, e. g., the enforcement of IPRs but also tax and tariff policies of the government. Especially in these two areas, suggestions from intermediary institutions have been considered by the government, whereas in other areas and other cases, the government did not take the critique into account. The communication process between government and intermediary institutions seems to be steadily improving and becoming more transparent. But there is always room for improvement, especially if the government wants to implement a modern industrial policy and export promotion, which takes the needs of export industries and enterprises into account.

Business associations already play an important role in distributing information about political decisions, legislative changes and regional and international integration. In these areas, they provide a range of training activities, e. g. on standards and norms on export markets or on the creation of new designs for the companies concerned. However, many enterprises complain about a lack of information and a lack of practical orientation of training facilities. Thus, further training facilities have to be developed in order to support the business sector adequately in competing in international markets. On the one hand, some intermediary institutions themselves lack information in their respective field of activity; for instance, many training institutions for standards and norms are not aware of the importance of product standards. On the other hand, many intermediary institutions lack financial resources to provide appropriate training facilities; for instance in the field of export promotion, there is still much room for improvement in terms of professional marketing, information, etc.

In a market economy, business associations and other intermediate institutions play a vital role in policy networks between government and industry



representatives. Effective communication channels are needed for developing a vision for Vietnam's industrial strategy and its future place in international markets that is shared by all stakeholders in Vietnam's economic modernisation, private industry, state owned enterprises, foreign investors and the government. If today many firms still do not make use of the potential role of business associations as information channels, a better publicity and further political independence seems to be needed so that intermediary institutions can play an effective role in shaping industrial policy in Vietnam. The government could support the development of independent intermediary institutions, particularly for export promotion activities, helping domestic firms to discover new export markets and informing foreign buyers about the potential of the Vietnamese enterprises and the domestic market.

### 6.1.3 Micro level: How to increase competitiveness?

Further development of already promising and vigorous private sector activities in Vietnam is still restricted through intransparent and unpredictable policy making of the government. Numerous formal and informal obstacles for business development through uneven treatment and lack of information prevent entrepreneurs from profitable investment. Some private enterprises already have the potential to become successful exporters if equal opportunities were provided and existing barriers to growth reduced.

However, Vietnamese *private businesses (mainly SME)* themselves could invest more time and effort in exploring foreign markets and developing new marketing activities and R&D geared to develop products suitable to the quality requirements of export markets. In particular, firms should learn more about the meaning and importance of IPRs and trademarks as marketing instruments. On the other hand, private business could influence government policy to a larger extent through intermediary institutions like business associations as communication channels.

Furthermore, a large number of *SOEs* are still relying on support and protection from the government. Due to trade liberalisation and cuts in subsidies, they will face severe adjustment problems with negative consequences for the banking sector and the labour market. The major challenge is to equitise the remaining *SOEs* against the opposition of strong lobby

groups in the government and SOEs themselves. However, some SOEs have already shown that profitable adjustments are possible.

The majority of FIEs in Vietnam strongly supports the efforts that are being made to establish a level playing field. However, some import-substituting FIEs in specific industries rely on government protection (e. g. in the automotive industry). They will have to adjust to increasing import competition and improve their international competitiveness. In general, FIEs play a vital role in the technology development of Vietnamese businesses but their links with private Vietnamese SMEs are still relatively weak. The government can play an important role in stimulating buyer-supplier relationships between FIEs and domestic ancillary industries by creating incentives for private enterprises to invest in new technologies and R&D to be able to meet the technical standards and quality requirements of the foreign enterprises.

Summing up, the analysis of the five areas for adjustment to WTO rules and other requirements for international economic integration shows that the uneven treatment of state-owned, private owned and foreign invested enterprises will be a major obstacle for a modern industrial policy emphasizing competition instead of protection and subsidies. The combination of high import tariffs and other import barriers with subsidies to state owned enterprises had created the typical anti-export bias of the traditional import substitution strategy. Both domestic and foreign enterprises producing for the protected domestic market had little incentive to venture into export marketing where profit margins are lower and risks are higher. The reduction of import tariffs and other import barriers required by WTO accession will remove the anti-export bias by increasing competition on the domestic market, which will force domestic industry to upgrade their product, and processing technologies and invest in R&D and quality improvement. Firms that are exposed to international competition on their home market will find it easier to meet the requirements of foreign buyers and to start their own export marketing activities. The government can support this by removing existing obstacles to efficient manufacturing and exporting and by providing the infrastructure and financial services needed for modern exports. In general, providing a level playing field for Vietnamese businesses means equal distribution of financial and other resources for investment, for example in technology, in R&D activities, in marketing etc. Then, investment decisions can be taken independently and competitive

industries may be able to develop. Therefore, reducing market entry barriers for different forms of enterprises through the provision of a level playing field accompanied by appropriate adjustment policies (e. g. a social security system etc.) is the most important step towards WTO accession and global integration of Vietnam.

Vietnam will not be able to follow the development path of its East Asian neighbours with a high degree of state intervention and strategic planning of economic development (Perkins 2001, 260). On the one hand, WTO rules simply restrict Vietnam from following the active industrial policy approach of the *East Asian Miracle* countries. On the other hand, it is an open question whether this would be the appropriate industrial policy approach for Vietnam in the present era of globalisation. The industrial policy strategy of the East Asian economies required a highly strategic approach to industrial policy making. It seems doubtful whether this strategic orientation can be achieved in Vietnam. In addition to that, in today's globalizing economy in which many developing countries have developed the same industries, strategic planning of industrial development for a latecomer like Vietnam would be even more demanding than for the front-runners of the East Asian Miracle. Vietnam's East Asian neighbours are also reforming their industrial policies with respect to WTO and the requirements of international production networks (Lall 2005). With the increasing importance of global production and marketing networks, the goal for industrial policy of developing countries can no longer be to develop fully integrated industries in one country, but to provide a suitable framework for enabling local producers – and foreign investors – to plug into these international production networks.

Therefore, the government may focus on the provision of a sound economic framework and an attractive investment climate with adequate adjustment policies in terms of social security, employment structure etc. and modern competition policy. This may replace specific “active” policy interventions that implicitly overestimate the planning capacity of the government. Based on this new focus, more intense exchange of ideas with different actors on the meso and the micro level could be fruitful for industrial policy making.

## 6.2 Possible Areas for Donor Activities

There can be no doubt that some important challenges for a successful integration into the global economy still remain for the Vietnamese government, the meso institutions and the business sector. The donor community already supports the Vietnamese efforts to a large extent and in various ways on the different levels (see below 6.3.2). In the following, some areas of technical assistance related to the five WTO topics discussed in this study are presented. The table below shows possible intervention areas for donors regarding trade-related measures in general. This study focuses on activities in the areas where implementing WTO obligations are required on the macro, meso and micro level (column 2), as well as on the improvement of trade capacities (column 3).

<b>Table 4: Intervention areas and levels for trade-related development cooperation</b>			
Intervention area of the donor community	Negotiating of multilateral trade agreements	Implementation of agreed obligations	Improvement of trade capacities
Macro level (government, ministries etc.)	Country specific consultation about the economic, social and political implications of negotiation issues; extension of the exchange between negotiation delegations from developing countries	Consultancy and training measures for administrative staff, e. g. working in the area of implementing the TRIPS Agreement	Consultancy to simplify export and import measures (e. g. customs clearance) in order to decrease transaction costs
Meso level (institutions)	Support of network co-operation between enterprises through workshops, establishment of round tables; support of	Support of associations and private service institutions to inform the domestic industries about the new challenges, e. g.	Creation of Consultancy Services to profit from new export opportunities; to increase the added value in the country by build-

	interest identification and articulation with the objective that the government is taking note of their concerns during negotiations	new ecological standards	ing up further processing industries
Micro level (enterprises)	Offering information about the issues of bi- an multilateral negotiations to increase transparency	Making information available about quality requirements resulting from new treaties, e. g. SPS measures	Support of partnerships with enterprises, which consult and teach providers in issues like design, quality safety, new production technologies
Source: BMZ (2004)			

Firstly, multilateral co-operation should focus on supporting *Vietnam's government institutions in order to implement WTO obligations on all administrative levels*. Consultancy and training measures for administrative staff in particular, should be strengthened. Taking the customs offices as an example, existing training programmes<sup>62</sup> have to be upgraded in accordance with international standards and experiences. Additionally, training facilities need to be improved to implement the required customs valuation system and to increase the know-how about the protection of intellectual property rights.

Secondly, the interviews revealed that a lot remains to be done in the *development of independent intermediary institutions like business associations or non-governmental Organizations* in order to enable them to inform domestic industries about new challenges through changing government policies on the one hand and to act as interlinking bodies to influence

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62 During the interviews, Vietnamese government officials as well as enterprises emphasised that they need practically oriented training courses and a better co-ordination of donor activities regarding the training measure in different areas, e. g. education on IPRs or standards and norms.

policy formulation on the other. Although many enterprises in Vietnam are organised in and represented by business associations, they still face a lack of knowledge about current changes in the trade regime of Vietnam: about the challenges they will face as well as about the benefits they might gain. On the one hand, this calls for building up adequate training facilities to inform enterprises in a practical manner. On the other hand, the institutions should be supported to develop a stronger voice and discover channels for representing the interests of the business sector more effectively at macro level institutions.

In the field of import policy, this would concern proposals from the business sector on tax reform, business registration procedures etc. to the relevant government institutions. In the field of enforcement of IPRs, newly established representative institutions like the Recording Industry Association of Vietnam or VIPA should be supported in order to ensure that their voices are taken into account regarding the formulation of laws and policies. In addition, the capacity of these meso institutions should be strengthened to support their efforts to raise public awareness about IPRs. In the area of export promotion, institutions like VCCI and export promotion agencies should be given support to actively encourage enterprises to export to foreign markets and advise private and state-owned companies in marketing issues. In addition, in the area of standards and norms, training courses and train-the-trainer seminars especially for the Investment and Trade Promotion Centre (ITPC) and STAMEQ should be increased. The courses should focus more on product standards and less on production process standards as the interviews showed a lack of awareness among enterprises of the importance of product standards for exporting. Efforts in this field should be strengthened so that ITPC and STAMEQ can spread the relevant knowledge among enterprises. Additionally, the awareness about the importance of reliable testing and certification institutions and independent accreditation institutions can thus be increased. In consequence, this may also pressure the Vietnamese testing, certification and accreditation institutions to improve their performance.

Thirdly, although some international support programmes on SME development have been implemented in the past, targeted *support for SME development* still seems to be needed. On the one hand it is advisable to build up quality oriented suppliers for private Vietnamese and foreign invested enterprises, e. g. in the area of textiles and garments. On the other

hand, this also means to support the government in removing existing barriers to growth for efficient SMEs so that they can reach international levels of economies of scale. Adequate measures for a better export performance of SMEs could be: better distribution of information about the requirements of export markets; improvement of marketing performance focusing on international markets, awareness raising among enterprises regarding the importance of IPRs, especially the registering of trademarks as a marketing instrument; training courses for companies about product standard requirements on international markets. In order to support enterprises in the latter area, donors could establish programmes to sponsor the implementation of product standards.

A major conclusion of this report is that the most important prerequisite for making Vietnam's industry capable of competing with increasing imports and finding new export markets will be to provide a level playing field for the different types of enterprises. Therefore, *SOE reform* is another important task in the field of business and private sector development in Vietnam. Not only the equitization process, but also the *development of adequate complementary adjustment policies* (social security policy, unemployment insurance, banking reform etc.) should be supported by multilateral co-operation projects.

### 6.3 The role of development assistance

Trade-related technical assistance will have to play an important role in facilitating Vietnam's adjustment to the multilateral rules-based system of the WTO and its integration into the global economy. Vietnam has already received a multitude of donor activities since the late 1990s supporting the preparations for WTO accession and the implementation of the obligations resulting from other regional and bilateral trade agreements. Some of these programmes will phase out before WTO accession, but there is an increasing awareness of both the Vietnamese government and the donors that once Vietnam will have become a WTO member, there will be even more need for capacity development and training. Reforms of legislation in accordance with WTO requirements will be only the first step, and most of the legislative reforms will have been achieved by the time of WTO accession, but the new laws will have to be enforced and trade-related institutional reforms implemented. Capacity building of the relevant institutions

and training of their staff, especially the judiciary applying the new legislation will require a wide range of technical assistance for quite some time. In addition to that, Vietnam will have to develop and implement the economic and social reforms necessary to enable its economy to meet the challenges of international competition, to make use of the new opportunities of improved access to global and regional markets, and to facilitate the structural adjustments resulting from international competition.

### 6.3.1 Donors' commitment to increase aid for trade in the Doha Round

The international conditions for increasing *aid for trade* are favourable. In November 2001, the Doha Ministerial Conference of the WTO launched a new round of multilateral trade negotiations. It was given the label *Development Round* to indicate that in this round for the first time, development issues would be given high priority on the agenda. Within the development issues, aid for trade is a central pillar. The Doha Ministerial Declaration states that “*that technical cooperation and capacity building are core elements of the development dimension of the multilateral trading system.*” (WTO 2001b, para. 38) This was reconfirmed in the *July 2004 package* by which the round was launched again after the failure of the Cancún Ministerial Conference in September 2003: “*The General Council recognizes the progress that has been made since the Doha Ministerial Conference in expanding Trade-Related Technical Assistance (TRTA) to developing countries and low-income countries in transition. In furthering this effort the Council affirms that such countries, and in particular least-developed countries, should be provided with enhanced TRTA and capacity building, to increase their effective participation in the negotiations, to facilitate their implementation of WTO rules, and to enable them to adjust and diversify their economies.*” (WTO 2004b, 2)

There is a growing consensus between the trade and the aid communities that trade liberalisation alone, as expected from the Doha Round and other regional or bilateral trade negotiations, will not automatically lead to increasing exports by all developing countries (Stiglitz / Charlton 2006). A host of supply-side constraints and bottlenecks prevent especially the less developed countries from expanding and diversifying their exports in response to more open markets of developed countries. There is even the



risk that they will face considerable adjustment costs from increasing import competition and from the erosion of trade preferences for their exports before they will be able to balance the costs of trade liberalisation through increasing exports. Therefore, trade policy has to be complemented by additional and more effective aid for trade in various forms. Basically, aid for trade aims at strengthening the role of developing countries, especially Least Developed Countries (LDCs), to play a more active role in multilateral trade negotiations, helping them to implement new obligations resulting from WTO negotiations, to adjust to changing international competition and to improve the supply-side capacities of their export sectors in order to benefit effectively from improved access to export markets. Encouraging developing countries to introduce social safety nets and adjustment measures for those negatively affected by increasing import competition is especially relevant for mobilising political support for active participation in multilateral trade negotiations. In principle, it should be possible to generate more resources for additional aid for trade because the gains to OECD countries from effective multilateral trade liberalisation resulting from a successful conclusion of the Doha Round would be higher than present overall aid budgets (Hoekman 2004; Hoekman / Prowse 2005, 20; Prowse 2005, 18).

In addition to the general case for more aid for trade, developing countries with preferential access to major OECD markets, especially the EU and the US, may claim compensation for the loss of preferences that will result from multilateral trade liberalisation. The lower the tariffs, the lower are the preference margins for those exporters who do not have to pay the MFN tariffs. Thus, trade preferences have the perverse effect of making the beneficiary countries interested in keeping tariffs in OECD countries high because only this gives them an advantage over MFN imports from countries without preferential access. This perverse incentive for a large group of countries could make negotiations on general trade liberalisation difficult, and therefore the OECD countries are advised to think about compensation for preference erosion through additional aid.<sup>63</sup> It is widely recognised today that trade preferences had limited effect in stimulating

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63 As a country that does not have special preferential access to OECD markets as many less developed countries have, Vietnam would benefit most from multilateral trade liberalisation which would bring Vietnamese exports on an equal footing to the same exports from preference receiving countries.

trade development and diversification especially for least developed countries. Market access is not the major problem for these countries, but the host of supply side bottlenecks and lack of competitiveness of export sectors. These problems will be solved, if at all, by effective aid programmes, and not through trade preferences which only prevent the beneficiary countries from joining a grand coalition with the more advanced developing countries for effective multilateral trade liberalisation.

Another motivation for increasing aid for trade could be to “buy” agreement from developing countries to a less ambitious outcome of the Doha Development Round than expected, e. g. in the field of agriculture. Of course, this possibility was explicitly rejected by a Special DAC Meeting on Aid for Trade on 27 October 2005: *“The challenge for the aid and trade communities is to use the momentum behind both the DDA and the MDGs to successfully conclude the Doha Round. Evidently, aid for trade should not be used as a compensation for a DDA outcome that falls short of its ambitions.”* (OECD/DAC 2005, para. 21) But the fact that this possibility is mentioned in an official OECD document shows that offering more aid could be an easy compromise to bring a development round to an end that does not meet the expectations of developing countries.

The WTO itself provides technical assistance, mainly in the form of training programmes for government officials, especially from least developed countries, countries in transition and accession countries. The larger part of total trade-related technical assistance is provided by bilateral OECD donors and the World Bank. Consequently, the Doha Ministerial Declaration states: *“We underscore the urgent necessity for the effective coordinated delivery of technical assistance with bilateral donors, in the OECD Development Assistance Committee and relevant international and regional intergovernmental institutions, within a coherent policy framework and timetable.”* (OECD/DAC 2005, para. 39)

In order to support coordination among bilateral and multilateral donors in the field of trade-related aid, a Trade Capacity Building Database (TCBDB) was launched by the Secretariats of the WTO and the OECD in November 2002. Based on this database, the 2005 WTO / OECD Joint Report on Trade-Related Technical Assistance and Capacity Building (TRTA/CB) calculates that the share of TRTA/CB in total aid commitments of OECD donors was 4.4 %, plus 25 % of total aid that is allocated to infrastructure, which also has an effect on trade development (WTO /

OECD 2005, 5). Thus, bilateral donors and multilateral agencies have become much more active in TRTA/CB over the last few years. Donors have become more “aware of the importance of TRTA/CB for development and poverty reduction”, and the dialogue between development and trade practitioners has strengthened. The major donors and multilateral agencies have pledged to increase their budgets for trade-related projects and programmes.

The Joint Report distinguishes between two main categories of TRTA/CB:

- *“Trade policy and regulations covers support to aid recipients’ effective participation in multilateral trade negotiations, analysis and implementation of multilateral trade agreements, trade policy mainstreaming and technical standards, trade facilitation including tariff structures and customs regimes, support to regional trade arrangements and human resources development in trade.*
- *Trade development covers business development and activities aimed at improving the business climate, access to trade finance, and trade promotion in the productive sectors (agriculture, forestry, fishing, industry, mining, tourism, services) including at the institutional and enterprise level.”* (WTO / OECD 2005, 7)

Activities in the field of infrastructure development are not included in the TRTA/CB database, because it would be impossible to define and calculate the contribution of infrastructure projects to trade development.

There is a special link between trade-related technical assistance and one of the negotiating issues of the Doha Development Round: **Trade facilitation** is one of the four new negotiating issues that were mentioned at the first WTO Ministerial Conference in Singapore, December 1996 to be further investigated and negotiated in a coming WTO round. The four *Singapore issues* were trade and investment, trade and competition policy, transparency in government procurement and trade facilitation. After the failure of the WTO Ministerial Conference in Cancún, September 2003, the first three Singapore issues were dropped from the Doha Development Agenda due to resistance of most developing countries to accept new commitments before some of the imbalances they saw as a result of the Uruguay Round would have been removed. Trade facilitation remained on the agenda because developing countries were convinced that they would benefit most from the removal of administrative trade barriers like intrans-

parent customs procedures, and from the simplification and harmonisation of international trade procedures, especially if they would be given technical assistance for the necessary reforms and capacity development, e. g. modernisation of customs procedures. *“Technical assistance and capacity building (TA/CB) for trade facilitation is defined as support for the ‘simplification and harmonisation of international trade procedures. Trade procedures include the activities, practices and formalities involved in collecting, presenting, communicating and processing data and other information required for the movement of goods in international trade.’ This definition excludes donor support for issues closely linked to trade facilitation, such as assistance for understanding and compliance with Sanitary and Phytosanitary Standards and Technical Barriers to Trade; transport and storage or revenue-enhancement reforms.”* (OECD 2005, 17–18)

Interestingly, the 2001 DAC Guidelines on ‘*Strengthening Trade Capacity for Development*’ diagnoses not only the usual lack of capacity on the side of developing countries to manage trade policy effectively and to make use of the opportunities of international trade liberalisation, but with respect to the scaling up of donor activities in trade-related development co-operation activities, the DAC sees the need for donors themselves to strengthen their own trade-related capacities. *“Donors need to enhance their range of skills and knowledge. Expertise in building institutions (public, private and hybrid) and consultative mechanisms will be especially important. So will that for nurturing policy and support networks. In addition, strengthening stakeholder consultation and policy co-ordination will require better facilitation skills, especially in the field – and greater understanding of multilateral and regional trade issues.”* (OECD 2001, 15)

The 2001 DAC Guidelines on ‘*Strengthening Trade Capacity for Development*’ underlines the need to integrate aid for trade activities into national development strategies, such as Poverty Reduction Strategies. They should be aligned with an inclusive trade policy dialogue in which the government, the private sector, academia and civil society identify the supply side problems to be tackled and the agenda for negotiating in the multilateral arena and in regional and bilateral trade negotiations. One problem seems to be that there is often a lack of leadership and ownership on the side of the recipient country because the trade ministries are less

powerful than the traditional planning ministries responsible for aid allocation and negotiations with the donors.

In 2005, the principles for effective cooperation between donors and recipient countries have been agreed with the *Paris Declaration on Aid Effectiveness*. It gives priority to partner country ownership and leadership, donor alignment and harmonisation, capacity development, managing for results and mutual accountability. These new principles for effective aid apply to trade-related technical assistance as well. Of course, the application of these principles requires high-level political will and commitment to reform on the side of the recipient country. The constituency for trade facilitation must be strengthened in partner countries, especially the business community. Both policymakers and stakeholders in trade facilitation must understand and agree upon the road map to trade facilitating reforms. Needs assessment must be done for each country to identify the specific national needs and circumstances and to align donor activities better with national development strategies. Dialogue forums between government, the customs authorities and other stakeholders must be used for aligning donor programmes with the needs and strategies of the recipient country. Since trade facilitation can make import and export activities more profitable, the business community participating in the programmes may bear at least part of the costs.

In Vietnam, donors and the government have agreed upon the same principles: At the Mid-term Consultative Group Meeting for Vietnam in Can Tho on June 2–3, 2005, the Government of Vietnam and the development partners agreed upon the principles of ownership, alignment harmonisation and simplification, managing for results and mutual accountability, as declared in the Hanoi Core Statement on Aid Effectiveness.

### 6.3.2 Overview of past and current technical assistance programs related to Vietnam's WTO accession

A first survey on donors' activities and good practices in capacity development for trade in Vietnam was done for a DAC workshop in May 2000 (OECD / DAC 2000). The report praises Vietnam for its dramatic trade policy changes during the last decade, but states that more reforms will have to be done on the way toward WTO accession. There was a lack of support institutions for Vietnamese exporters, especially since it was diffi-

cult to establish private sector business associations. In view of the obstacles to exporting and the lack of institutional support, the rapid growth of Vietnam's exports was seen as *“even more surprising.”* (page 10) The reasons given in the report for Vietnam's export miracle are worth quoting here: *“Several factors seem to account for this competitive advantage: a strong work ethic, relatively high levels of education, a willingness to focus on the longer term, and high levels of entrepreneurship. In light of the substantial obstacles that government policies still pose to exports, Vietnam's recent trade performance is testimony to the resourcefulness and improvisational skills of Vietnamese entrepreneurs.”* (OECD / DAC 2000, 12)

The report presents an overall positive assessment of donor performance in the trade-related technical assistance programmes. It underlines the fact that Vietnamese officials take their own decision on trade policy matters independent of the donors' and their consultants' advice. In view of their historical experience, the Vietnamese take pride in arriving independently at the right decisions. And there is unanimous support from all donors for Vietnam's policy of gradually opening its economy to international competition, foreign direct investment and export orientation within the framework of ASEAN, of the bilateral trade agreements with the US and the EU and, finally, its decision to apply for WTO membership. On the basis of a common understanding of Vietnam's needs for trade-related technical assistance and capacity building, donor co-ordination was reported to be excellent, with several consultative group meetings, some of which reaching out even to the business community and to NGOs. Donor coordination was facilitated by the fact that there is strong recipient country ownership for aid projects and programmes in Vietnam, and the projects are selected by the Vietnamese according to their real needs. A major problem was getting Vietnamese private business involved. There seems to be a general suspicion among Vietnamese government officials of the motives of private entrepreneurs preventing to see them as the most important agents for a successful export drive. *“...in fact, Vietnam's private sector suffers from a serious image problem. The general public does not trust the entrepreneurs who open and operate the country's new private companies and is consistently ready to think the worst of them.”* (OECD / DAC 2000, 20)

The Vietnam Partnership Report 2005 (World Bank Hanoi 2005) contains a 12-pages table (65–76) listing no less than 80 trade related technical assistance (TA) programs of bilateral donors and multilateral agencies – including two by an NGO (OXFAM) – that have been implemented since 1999 or are planned for the coming years. The projects range from single activities like workshops to multi-year training programmes for Vietnamese officials in the various ministries and government agencies concerned with WTO-related issues. Their objectives are to improve the capacity of Vietnam's administration to implement the various legal and institutional reforms required for WTO membership, to help Vietnam's policy makers assessing the implications of WTO rules and agreements for economic development and poverty reduction, and to strengthen the capacity of Vietnam's agricultural and industrial producers / exporters to understand and adjust to the requirements of export markets, in particular through strengthening the capacity of Vietnam's standards and certification bodies to carry out the necessary testing and certification of export products.

The synopsis of trade- and WTO-related donor activities shows a wide array of themes and areas of support for capacity development. The need for trade-related assistance will not end with Vietnam's WTO accession. Even if most of the new legislation and adjustments of existing legislation in accordance with the rules and agreements of the WTO will have been done by 2007, it will be a long and arduous way to implement them effectively. The lack of capacity for dealing with the new challenges of WTO rules and of international competition will require training programmes for the various ministries and government agencies involved, but they should also include the business community with its associations and other civil society Organizations, and the universities and research institutes. There is a general need for integrating trade policy matters and issues of economic globalisation in the curricula of economics and law faculties of Vietnamese universities and academies. The judiciary in particular needs training in many new areas of commercial law and intellectual property protection. There will be a special and urgent need for training and capacity building in the area of technical standards (safety, health, environment) for export products, because these will be the major barriers to entry into export markets for Vietnamese products.

As a legacy from the socialist central planning era, there seems to be a lack of communication between the government and the business commu-

nity and civil society about the implications of globalisation and WTO membership and other trade agreements like ASEAN or bilateral trade agreements with the US and the EU. In the socialist era the government had exclusive control of foreign trade, and until today, trade policy has remained the domain of the central government and the Communist Party. In an open economy, however, trade policy, especially with the new agreements on agriculture, on services and on intellectual property rights, has implications not only for exporters and import competing industries, but also for almost every Vietnamese (e. g. intellectual property protection). This will have to be reflected in trade policy making.

Vietnam will have to broaden the constituency for trade policy making. It can no longer be defined and implemented by the Commerce Ministry alone, other ministries have to be involved, but what is more important, the business community and other civil society groups that have a stake in trade-related economic policy making, will have to be involved too. There is a need to establish and improve communication channels and forums for exchange of information between the government and the business community and other social groups, so that the government develops a clearer understanding of the views and interests of the business community and other groups with respect to trade policy matters; the reverse flow of information from the government to the business community is no less relevant for the companies' early preparation for changes in the conditions for international competition (Stiglitz / Charlton 2005, 168). Therefore, the capacity development and training programmes supported by technical assistance will have to include the business community with its associations, the trade unions and other civil society groups.

The donors can encourage the development of an inclusive system of discussion on trade policy matters. This is also the result of a new needs assessment commissioned by the Delegation of the European Commission in Vietnam. The report states as a central finding, *“that the contribution of business, research and civil society to trade policy formulation is very weak. Without a systematic and open dialogue between decision makers and other players, Government bodies cannot dispose of all information which is needed for optimal trade policy decisions.”* (European Commission, Delegation Hanoi 2005, 10) If the business community and their associations and other civil society associations will have to contribute effectively to the debate on trade policy and to defining Vietnam's posi-



tion in WTO negotiations and negotiations on other trade agreements, they will also need capacity building assistance and training programmes from donors.

Therefore, both donors and the Vietnamese government should think of complementing the technical and technocratic elements – which will be the core of the capacity building and training programs – with some form of awareness raising programmes (or programme elements) which give room to a critical discussion of the present state of globalisation and of the trade policy framework as represented not only by the WTO but also by regional and bilateral trade agreements. By inviting representatives of the business communities, trade unions and other civil society groups from the developed countries to workshops and training programmes with Vietnamese officials and representatives of the respective Organizations, the Vietnamese would better understand what forces are shaping the multilateral trade policy, why trade unions in the West demand social standards to be incorporated into the WTO system, and why civil society Organizations demand new and ever more stringent health, safety and environmental standards and norms for all products on the market which leads to the difficulties of compliance for exporters in developing countries. Debating face to face with representatives of different interest groups from developed countries about the challenges and opportunities of globalisation and about the importance of rules to establish conditions for freer and fair trade would create a deeper and more realistic understanding of the common challenges of globalisation and of the multilateral trading system.

A special theme for international workshops, seminars and training programmes for Vietnamese officials and business representatives could be the remaining (*industrial*) *policy space* under the WTO. How do other countries define their industrial policy objectives, what measures do they apply, and what conflicts have they experienced with trade interests of other countries? In this area it would be especially relevant for Vietnamese officials to learn from the experience of the more advanced East Asian countries who had to adjust their active and selective industrial policies to the narrower policy space as defined by the new WTO agreements and general trade liberalisation obligations. A special lesson to be learnt from the successful East Asian industrialising countries like South Korea, Taiwan, Thailand or Malaysia would be how these countries have organised an efficient dialogue between industrial policy makers in the government

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and specialised government agencies on the one hand and the business community on the other.



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## **Appendix**





	China (2001)	Indonesia (2001)	Malaysia (2001)	Philippines (2001)	Thailand (2002)	Vietnam (Sept. 2003)
Total lines	5,098	5,110	5,106	5,112	5,056	10,689
Tariff bands	57	52	45	38	45	16
Range tariff	1-122	0-170	0-1195	0-60	0-80	0-150
Average tariff	17.48	8.43	10.2	7.6	18.48	18.53
Dispersion rate (CV)	71.3	127.8	340.3	93.9	84.4	120.78
Source: Athukorala (2004, 76)						

Task	Distribution of firms by the difficulties encountered*		
	Not at all	Somewhat	To an important degree
Obtaining import licences	58.5	36.6	4.9
Custom procedures	27.3	58.0	14.7
Port service	63.4	30.5	6.1
Duty rebate	42.9	32.5	24.6
Source: Athukorala (2002, 49) Note: * Excluding non-respondent firms			

<b>Export items</b>	<b>1997</b>	<b>1998</b>	<b>1999</b>	<b>2000</b>	<b>2001</b>	<b>2002</b>	<b>2003</b>
Crude oil	15.6	13.2	18.1	24.2	20.8	19.6	19.0
Coal	1.2	1.1	0.8	0.7	0.8	0.9	0.9
Rubber	2.1	1.4	1.3	1.1	1.1	1.6	1.9
Rice	9.5	10.9	8.9	4.6	4.2	4.3	3.6
Coffee	5.4	6.3	5.1	3.5	2.6	1.9	2.5
Marine products	8.6	9.2	8.4	10.2	11.8	12.1	10.9
Garments	16.4	15.5	15.1	13.1	13.1	16.5	17.9
Footwear	10.7	11.0	12.0	10.2	10.4	11.2	11.2
Handicrafts	0.7	0.7	1.2	1.0	1.6	2.0	2.0
Electronic goods and components	4.8	5.3	5.1	5.5	4.0	2.9	4.2
Other	27.2	21.3	24.0	25.9	25.1	23.0	25.9
Source: IMF (2003, Tab. 25); IMF (2006, Tab. 24)							

<b>Continent</b>	<b>Percentage of total export value</b>
Asia	48.3 %
America	22.3 %
Europe	21.4 %
Australasia	7.5 %
Africa	0.5 %
Source: CIEM (2004, 22)	

**Table 5: Nominal tariff rates and dispersion in selected East Asian countries (in per cent)**

	China (2001)	Indonesia (2001)	Malaysia (2001)	Philippines (2001)	Thailand (2002)	Vietnam (Sept. 2003)
Total lines	5,098	5,110	5,106	5,112	5,056	10,689
Tariff bands	57	52	45	38	45	16
Range tariff	1-122	0-170	0-1195	0-60	0-80	0-150
Average tariff	17.48	8.43	10.2	7.6	18.48	18.53
Dispersion-rate (CV)	71.3	127.8	340.3	93.9	84.4	120.78

Source: Athukorala (2004, 76)

**Table 6: Granted patents for inventions between 1990 and 2001**

Year	To Vietnamese	To foreigners	Total
1990	11 (62)*	3 (17)	14 (79)
1991	14 (39)	13 (25)	27 (64)
1992	19 (34)	16 (49)	35 (83)
1993	3 (33)	13 (194)	16 (227)
1994	5 (22)	14 (270)	19 (292)
1995	3 (23)	53 (659)	56 (682)
1996	4 (37)	58 (971)	62 (1008)
1997	0 (30)	111 (1234)	111 (1264)
1998	5 (25)	343 (1080)	348 (1105)
1999	13 (35)	322 (1107)	335 (1142)
2000	10 (34)	620 (1205)	630 (1239)
2001	7 (52)	776 (1234)	783 (1286)
Total	94 (426)	2342 (8045)	2436 (8471)

Source: NOIP (2002, 46) \*Numbers in parenthesis are the application numbers

<b>Table 7: Granted patents for utility solutions between 1990 and 2001</b>			
<b>Year</b>	<b>To Vietnamese</b>	<b>To foreigners</b>	<b>Total</b>
1990	23 (39)*	0 (25)	23 (64)
1991	44 (52)	1 (1)	45 (53)
1992	23 (32)	1 (1)	24 (33)
1993	9 (38)	1 (20)	10 (58)
1994	18 (34)	9 (24)	27 (58)
1995	8 (26)	16 (39)	24 (65)
1996	5 (41)	6 (38)	11 (79)
1997	8 (24)	12 (42)	20 (66)
1998	3 (15)	14 (13)	17 (28)
1999	6 (28)	12 (14)	18 (42)
2000	10 (35)	13 (58)	23 (93)
2001	17 (35)	9 (47)	26 (82)
<b>Total</b>	<b>174 (399)</b>	<b>94 (322)</b>	<b>268 (721)</b>
Source: NOIP (2002, 47) *Numbers in parenthesis are the application numbers			

<b>Table 8: Granted patents for industrial designs between 1990 and 2001</b>			
<b>Year</b>	<b>To Vietnamese</b>	<b>To foreigners</b>	<b>Total</b>
1990	91 (194)*	9 (6)	100 (200)
1991	219 (420)	5 (2)	224 (422)
1992	433 (674)	6 (14)	439 (688)
1993	528 (896)	21 (50)	549 (946)
1994	524 (643)	27 (73)	551 (716)
1995	626 (1023)	85 (108)	711 (1131)
1996	798 (1516)	68 (131)	866 (1647)
1997	261 (999)	62 (157)	323 (1156)
1998	728 (931)	94 (126)	822 (1057)

1999	841 (899)	94 (137)	935 (1036)
2000	526 (1084)	119 (119)	645 (1203)
2001	333 (810)	43 (242)	376 (1052)
<b>Total</b>	<b>5908 (10089)</b>	633 (1165)	6541 (11254)
Source: NOIP (2002, 50) *Numbers in parenthesis are the application numbers			

<b>Table 9: Registered trademarks between 1990 and 2001</b>			
<b>Year</b>	<b>To Vietnamese</b>	<b>To foreigners</b>	<b>Total</b>
1990	423 (890)*	265 (592)	688 (1482)
1991	1525 (1747)	388 (613)	1913 (2360)
1992	1487 (1595)	1821 (3022)	3308 (4617)
1993	1395 (2270)	2137 (3866)	3532 (6136)
1994	1744 (1419)	2342 (2712)	4086 (4131)
1995	1627 (2217)	2965 (3416)	4592 (5633)
1996	1383 (2323)	2548 (3118)	3931 (5441)
1997	980 (1645)	1506 (3165)	2486 (4810)
1998	1095 (1614)	2016 (2028)	3111 (3642)
1999	1299 (2380)	2499 (1786)	3798 (4166)
2000	1423 (3483)	1453 (2399)	2876 (5882)
2001	2085 (3095)	1554 (3250)	3639 (6345)
<b>Total</b>	<b>16466 (24678)</b>	<b>21494 (29967)</b>	<b>37969 (54645)</b>
Source: NOIP (2002, 53) *Numbers in parenthesis are the application numbers			

<b>No</b>	<b>Date</b>	<b>Place</b>	<b>Organization</b>	<b>Interview Partner</b>
01	19.02.04	Hanoi	German Embassy	Katrin Oellers-Reis
02	19.02.04	Hanoi	GTZ	Dr. Monika Midl
03	19.02.04	Hanoi	CIM	Thomas Ganslmayer
04	19.02.04	Hanoi	GTZ-SME-Projekt	Corinna Kuesel
05	23.02.04	Hanoi	Oxfam	Eduardo Klien
06	24.02.04	Hanoi	KfW	Dr. Klaus Mueller
07	24.02.04	Hanoi	DIHK/AHK, Hanoi	Mr. Le Thanh
08	25.02.04	Hanoi	CIEM	Mr. Thanh
09	25.02.04	Hanoi	EU	Joachim Leckscheidt
10	25.02.04	Hanoi	CIEM	Dr. Cung
11	26.02.04	Hanoi	CIEM	Dr. Tran Tien Cuong
12	26.02.04	Hanoi	EU Delegation	Mr. Felipe Palacios Sureda
13	26.02.04	Hanoi	Advisor to the MPI-Minister	Mr. Le Dang Doangh
14	27.02.04	Hanoi	Social Security	Le Thi Hong Phuong
15	27.02.04	Hanoi	NCIEC	Mrs. Le Thi Huong Giang, Mr. Nguyen Son
16	27.02.04	Hanoi	German Embassy	Dr. Oliver Schnakenberg
17	01.03.04	Hanoi	Institute of Economics	Dr. Ha Huy Thanh
18	01.03.04	Hanoi	Institute of World Economy	Prof. Do Duc Dinh
19	01.03.04	Hanoi	Foreign Investment Agency (FIA), MPI	Dr. Nguyen Anh Tuan
20	02.03.04	Hanoi	MoT, Vice-Minister	Mr.Loung Van Tu
21	02.03.04	Hanoi	MPI	Mr. Dr. Nguyen Le Trung
22	02.03.04	Hanoi	MPI	Mr. Tran Hong Ky

23	03.03.04	Hanoi	HUAIC	Mr. Thai
24	03.03.04	Hanoi	Vietnam Cooperative Alliance	Mr. Dr. Nguyen Tien Quan
25	03.03.04	Hanoi	VCCI, SME	Mrs. Hang
26	04.03.04	Hanoi	Ministry of Industry	Mr. Huynh Dac Thang
27	04.03.04	Hanoi	DEG	Mrs. Daniele Soehngen
28	04.03.04	Hanoi	USAID, Star Project	Mr. Steve Parker
29	05.03.04	Hanoi	Garment Factory No. 10	Mr. Dang Phuong Dzung
30	08.03.04	Hanoi	Lisohaka Motor Joint Stock	Mr. Vu Manh Ha
31	09.03.04	Hanoi	Computer Communication (CMC)	Mr. Hà The Minh
32	09.03.04	Hanoi	Baker&McKenzie	Mr. Oliver Massmann
33	09.03.04	Hanoi	Xuan Kien Automobiles	Mr. Huyen
34	10.03.04	Hanoi	Mekong Economics. Ltd	Mr. Adam McCarthy
35	11.03.04	Hanoi	Copyright Department, MOCI	Mr. Do Khac Chien
36	11.03.04	Hanoi	Vinexad	Ms. Pham Thi Hai Yen
37	12.03.04	Hanoi	NOIP, MOST	Mr. Tran Quia Khanh, Mrs. Nguyen Thi Than Ha
38	12.03.04	Hanoi	EU-Mutrap	Mrs. Hang
39	15.03.04	HCMC	ITPC	Mr. Le Truong Son; Mrs Nguyen Thi Ngan Giang
40	15.03.04	HCMC	German Consulate	Mr. Winkler
41	16.03.04	HCMC	TÜV Rheinland	Mr. Klaus Ehret
42	16.03.04	HCMC	Young People's Business Association	Mr. Tran Thanh Binh
43	16.03.04	HCMC		Mr. Cuu
44	17.03.04	HCMC		Dr. Nguyen Chon Trung,



45	17.03.04	HCMC	Vietgoods	Nguyen Duy Thuan
46	18.03.04	HCMC	European Chamber of Commerce in Vietnam	Mr. Chris Wijnberg
47	18.03.04	HCMC	KarstadtQuelle	Mrs. Guhlmann
48	19.03.04	HCMC	German Business Ass.	Mr. Bischoff
49	19.03.04	HCMC	Meeting between HCMC People's Committee and Consulting Companies	
50	19.03.04	HCMC	Nidek TOSOK (Viet Nam) CO., LDT	Mr. Kunihiko Nishihara, Mr. Dao Thanh Quyet
51	22.03.04	HCMC	STAMEQ	Dr. Nguyen Huu Thien
52	22.03.04	HCMC	ITPC, Trade Promotion	Mr. Vu Xuan Duc
53	22.03.04	HCMC	Department of Science and Technology of HCMC	Mrs. Hoang To Nhu
54	22.03.04	HCMC	Former Vice Director Artex Vietnam	Mr. Nguyen Ngoc Tho
55	22.03.04	HCMC	Translator	Dr. Nguyen Ngoc Tho
56	23.03.04	HCMC	Euroasiatic	Mr. Hetzert
57	23.03.04	HCMC	Freetrend	Mr. Chen
58	23.03.04	HCMC	adidasSalomon	Mr. Joel Enderle
59	24.03.04	HCMC	Association of Garment-Textile-Embroidery-Knitting	Mr. Bui Trong Nguyen
60	24.03.04	HCMC	VCCI, Patent and Trademark Bureau	Mrs. Vo Thi Minh Tam
61	24.03.04	HCMC	Stinnes Logistic	Mr. Braunbach
62	24.03.04	HCMC	KD Feddersen	Mr. Stechmann
63	24.03.04	HCMC	Mountech	Mr. Thuere
64	24.03.04	HCMC	VCCI, Deputy General Director	Mr. Nguyen The Hung
65	25.03.04	HCMC	VCCI, Trade Promotion	Mr. Nguyen Thanh Binh

66	25.03.04	HCMC	Artex Saigon	Mr. Canh
67	25.03.04	HCMC	Mekong Auto	Mr. An
68	25.03.04	HCMC	Business Women Club	Mrs. Nguyen Thi Huong et al
69	26.03.04	HCMC	Huy Hoang Garment	Mr. Le Nu Thuy Duong
70	26.03.04	HCMC	Saigon High Tech Park	Mr. Pham Chanh Truc
71	26.03.04	HCMC	Amanda Foods	Mr. Emmanuel Anton
72	26.03.04	HCMC	Anam Electronics (VN) Ltd	Mr. Beat H. Waefler
73	29.03.04	HCMC	Taphuco Textiles and Garments	Mr. Nguyen Van Thuy
74	29.03.04	HCMC	Cholimex	Mrs. Tran
75	29.03.04	HCMC	Sadaco	Mrs. Nguyen Thi Tram
76	29.03.04	HCMA	Digitexx	Mr. Schellenberg
77	29.03.04	HCMC	Minh Dat Textiles	Mr. Kha Duc
78	01.04.04	HCMC	People's Committee	Dr. Nguyen Thien Nhan
79	01.04.04	HCMC	SES	Mrs. Nguyen Thi Minh Phuong
80	05.04.04	HCMC	Mercedes-Benz	Mr. Rapp
81	08.04.04	Hanoi	Vitas	
82	14.04.04	Hanoi	VIPA	Mr. An Khang
83	19.04.04	Hanoi	ADB	Mr. Ramesh Adhikari
84	19.04.04	Hanoi	Ministry of Foreign Affairs	Mrs. Nguyen Hong Bac, Mr. Chu Cong Hoang
85	19.04.04	Hanoi	World Bank	Mr. Klaus Rohland
86	23.04.04	Hanoi	Ministry of Industry	Dr. Cao Quoc Hing
87	27.04.04	Hanoi	Ministry of Industry	Mr. Hoa
88	27.04.04	Hanoi	Ministry of Finance	Mr. Dang Tuan Hiep

<b>Table 11: Time schedule of the research period in Vietnam</b>		
<b>Time</b>	<b>Place</b>	<b>Activities</b>
17.02.2004	Hanoi	– Arrival in Vietnam
18.02.–12.03.2004	Hanoi	– General orientation and introduction – Testing of questionnaire material with counterpart – Interviews with ministry employees, meso level institutions, enterprises and donors
12.03.–05.04.2004	Ho Chi Minh City	– Interviews with meso level institutions, enterprises – Analysis and interpretation of interview results
05.04.–27.04.2004	Hanoi	– Interviews with ministry employees and meso level institutions – Finalising summary of findings – Preparation of two workshops on the basis of the results
28.04.2004	Hanoi	– Presentation of results to the Ho Chi Minh Political Academy
29.04.2004	Hanoi	– Presentation of results to CIEM and other Vietnamese stakeholders and donors
30.04.2004	Hanoi	– Departure from Vietnam
03.05–31.05.2004	Bonn	– Final draft period
25.05.2004	Bonn	– Presentation of report at the GDI

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