THE DRIVING FORCE OF INTERNATIONAL TRADE IN VIETNAM ECONOMY

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International trade has a significant role in Vietnam's present economy as the country accelerates its transition to the modern market economy as well as deeper and wider integration into global economy. Export in particular has proven instrumental in economic recovery and resilient in facing the challenges as a part of the world's economy – still subdued by the global financial crisis and economy recession since 2008.

In this paper, we will attempt to address the importance of international trade, especially the role of export as the driving force behind Vietnam's resilience and growth in recent years and discuss the measures to strengthen export performance in contributing to the sustainable economic development of Vietnam.

Export Performance – the Engine of Economic Growth of Vietnam Today

The contribution of international trade to the economic growth of Vietnam can be both direct and indirect.

In principle, export/import activities create more jobs and income to an economy. International trade can also redirect investment towards the most profitable sectors of the economy, thus making investment more efficient. Moreover, international trade expansion may lead to an improvement in national productivity as well as encourage institutional and administrative reform that strengthens the international competitiveness of the examined economy.

In recent years, international trade activities in Vietnam have considerably contributed to Vietnam's economic and social development. Export has become one of the key factors in economic growth, increasing employment, raising income, helping eliminate and alleviate hunger and poverty.

As a country lacking advanced economic and technology tools, Vietnam has benefited greatly from import: it provides Vietnam with access to new and advanced technology, which more than compensates for the lack of domestic sources of materials, intermediate input, equipment and machinery and consumer goods. In general, import has contributed to strengthening production and export power, improving technological dimensions, stabilizing macroeconomic. It also supports a safe and organized life: Vietnamese people are now able to choose from an abundant source of quality goods and services at competitive prices, etc.

The importance of international trade can be measured by the ratio of export/import over gross domestic product (GDP), the growth rate of import/export in comparison with GDP and the percentages/portions of import/export to GDP growth rate, etc. The impact of international trade on Vietnam's economy can be examined through the structural changes of trade, trade balance, foreign exchange reserves, foreign debt of Vietnam as well as the movement of domestic commodity prices and inflation, the reduction in hunger and poverty, and environmental improvement or deterioration, etc.

Table 1.

International trade and economic growth of Vietnam in the period of 2001-2012.

Unit: mil.US$; %

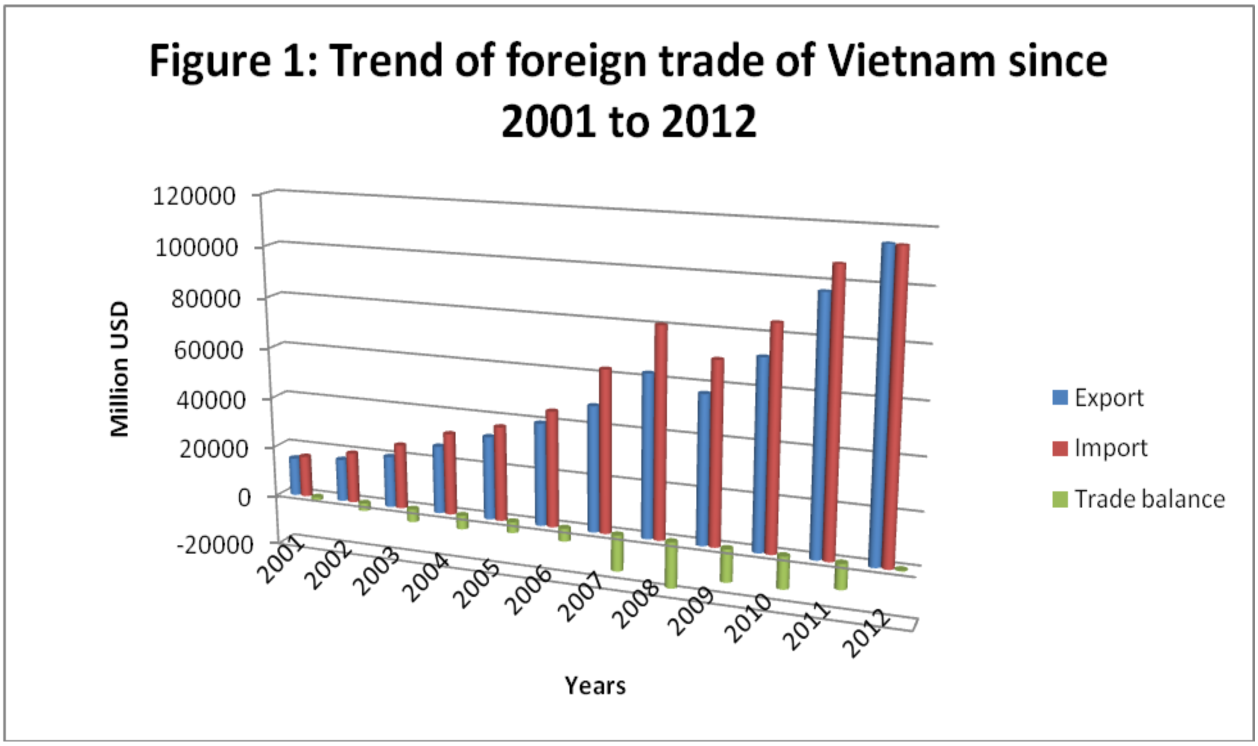
Years	GDP	GDP growth rate	Merchandise Export	Export growth rate	Export / GDP	Merchandise Import	Import growth rate	Import/ GDP	Trade balance	TB on Export
2001	32,650	6.8	15,027	3.8	46.0	16,218	3.72	49.7	-1,189	7,9
2002	34,130	7.04	16,705	11.2	47.7	19,746	21.75	57.9	-3,040	18,2
2003	38,830	7.24	20,149	20.6	53.0	25,256	27.90	65.1	-5,107	25.34
2004	45,270	7.7	26,504	31.5	57.7	31,954	26.52	70.6	-5,450	20.56
2005	52,700	7.5	32,233	21.6	60.3	36,761	15.04	69.8	-4,314	13.3
2006	60,860	7.4	39,605	22.1	65.5	44,891	22.12	73.8	-5,065	12.7
2007	71,470	8.48	48,400	21.5	67.9	62,765	39.82	87.8	-14,204	29.25
2008	90,620	6.18	62,900	29.5	70.0	80,714	28.60	90.1	-18,029	28.76
2009	97,210	5.32	57,096	-9.7	60.8	69,949	-13.34	74.5	-12,853	22.5
2010	106,570	6.78	72,236	26.5	72.2	84,839	21.23	81.9	-12,609	17.46
2011	123,600	5.89	96,905	34.1	78.6	106,749	25.82	86.4	-9,844	10.16
2012	141,700	5.25	114,631	18.3	80.9	114,347	7.1	80.7	284	0.2

Sources: GSO, MOIT Vietnam, IMF, WB

In examining the structural changes of trade of Vietnam during the period of 2001-2012, it can be seen that the volume of trade of Vietnam has increased rapidly. According to the trade statistics of the General Statistics Office – GSO of Vietnam, Vietnam’s total value of merchandise export (in nominal US. Dollars) increased from USD 15 billion in 2001 to USD 114.63 billion in 2012, reaching an average growth rate of 20.3% per year in the period of 2001–2012. This led to a rise in Vietnam’s share in global export, from 0.24% in 2001 to 0.62% in 2012. Vietnam’s total merchandise import value rose from USD 16.2 billion in 2001 to USD 114.34 billion in 2012, reaching an average growth rate of 19.4% per year during the same period. This caused Vietnam’s share in the global import to increase – from 0.26% in 2001 to 0.61% in 2012. In the end of this period, Vietnam claimed its position as the 37th exporter and 33th importer of the world in 2012. The strong export performance continued throughout 2013 with total export value estimated to have grown by 16% during the first eleven months of 2013 and reached USD 121 billion at the end of the November 2013.

Regarding commodity export/import structures of Vietnam during the period between 2001 and 2012, there was no significant changes in commodity structures. Vietnam mainly exported commodities such as raw materials, fuels, agricultural, forest, aquatic products and other labor-intensive products while importing mainly manufactured goods such as equipment and machinery, intermatdiate input and materials for export processing, consumer goods, etc. However, since 2011, the commodity export structure has been changing a lot.

Apart from the traditional labor-intensive manufacturing exports such as garments, footwear, and furniture which continued to grow steadily, there have been notable additions to the export composition: hi-tech and high-value products, for example, cell phones and parts, computers, electronics and accessories, automobile parts… They have emerged as the largest and fastest-growing export items in 2013, signaling of an export structure change toward hi-tech, high and value added manufactures. The solid export performance is largely attributed to the foreign-invested sector, which now accounts for two third of Vietnam's total exports.



Sources: Import, export statistics, MOIT Vietnam

In spite of national efforts to diversify and expand new markets for import/export, Vietnam's import/export market shares have seen little change during the period of 2001-2012. Vietnam now has commercial relations with more than 225 countries and territories over the world. However, among them, 15 main commercial partners hold more than 80% of Vietnam's total value of import and export. They are the United States, Japan, members of EU-27, Australia, China, and NIEs of Asia such as South Korea, Taipei, Hong Kong and Singapore and other members of ASEAN. Currently, 10% of the total export markets of Vietnam (20 largest export markets) account for 80% of the Vietnam's total export value while the remaining 90% account for only 20% of Vietnam's total export value. Five biggest clients of Vietnam export which accounted for 63% of Vietnam's total export value in 2012 were the U.S. (17.5%), EU27 (17.1%), China (12%), Japan (11.4%) and Republic of Korea (5%). Regarding the supplier markets of Vietnam, China is the biggest one with a share of

25% of Vietnam's total import value in 2012. The other main suppliers of Vietnam are South Korea, Japan, Taipei, Singapore, Thailand, etc, as shown in the figure 2.

Figure 2a: Import market share of VN in 2001 (%)

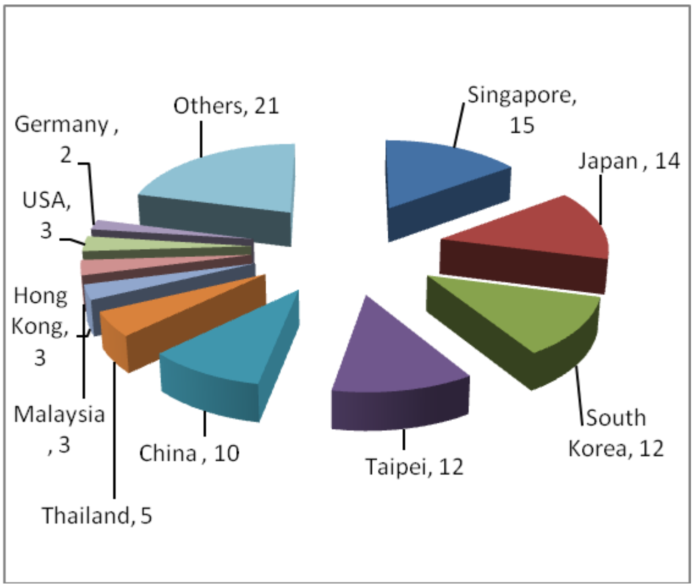
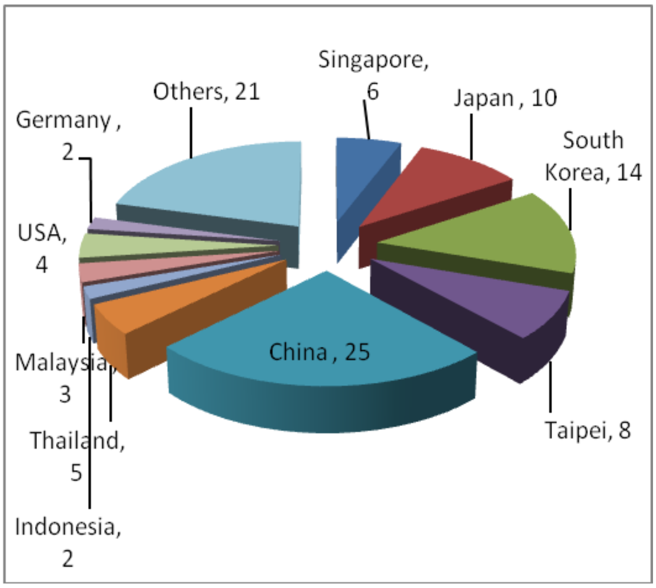


Figure 2b: Import market share of VN in 2012 (%)

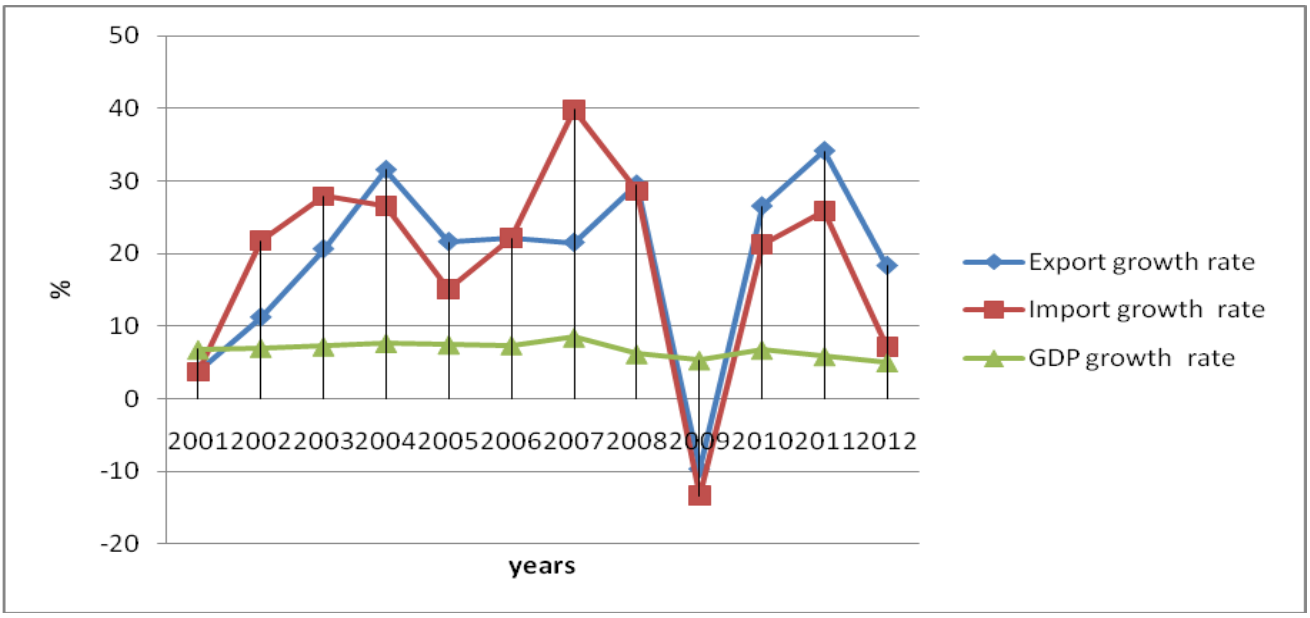


Source: MOIT Vietnam 2001, 2012

In order to understand the importance of international trade, especially export, in Vietnam's economy, one should consider the volume of import/export in comparison to the GDP of Vietnam. Table 1 shows that the ratio of export/import to GDP increased in the period 2001-2012. The total value of export that accounted for 46% of GDP in 2001 increased to 80.8% of GDP in 2012. The respective values for import during this period were 49.7% and 80.7%. With the trade to GDP ratio of 161.5% in 2012, the openness of Vietnam economy is very large. On one hand, international trade has great importance, but it also puts Vietnam's economy to a more vulnerable and riskier position should it face any shock from the world market.

When it comes to the growth rate of import/export in comparison with the GDP, figure 3 shows that export/import has grown faster than GDP in the period of 2001-2012, except for 2001 and 2009 when international trade was seriously affected by the regional and global financial crisis. The growth rate of export was generally 1.5-3.5 times greater than that of GDP and has been exceeding import since 2010. This led to a surplus in trade balance in 2012 and cemented the role of export as the driving force of economic growth in recent years.

Figure 3: Export/import and GDP growth rate of Vietnam in the period of 2001-2012



Sources: GSO, MOIT Vietnam

In order to further analyze the percentages of exports to GDP growth rate, one can apply the following basis equation of national accounts:

$$Y = I + C + X - M$$

Where Y denotes Gross Domestic Product by expenditure category; I denotes Gross capital formation (include gross fixed capital formation and changes in stocks); C denotes final consumption (include State and private consumption); X-M denotes trade balance (goods and services).

As the equation points out, GDP growth depends on three variables: I, C and Net Export. Table 2 shows the contribution of net export to GDP growth rate besides gross capital formation and final consumption. Therefore, export's contribution to GDP has been much higher than GDP growth itself, especially since 2005. This resulted from the strong export performance of Vietnam in the last 12 years: the speed of export is always higher than GDP and the ratio of export to GDP gets bigger and bigger. However, the much higher import growth rate had damped the contribution of net export to economic growth in the period of 2001-2010. In the couple years of 2011 and 2012, the condition was reverse, the much slower import speed and the strong export growth brought about great contribution of net export to GDP growth. Net exports have actively compensated the sluggish final consumption and less gross capital formation as the main engine to Vietnam economic growth. Net exports contributed 2.96 percent points in 5.03 percent points of GDP growth rate in 2012. Furthermore, these findings only based on the statistics, the more comprehensive and systematic approach on international trade should strongly reaffirm the driving force of export to Vietnam economic growth, especially Vietnam is still a lower middle income country with limited domestic purchase power, the import demand of the world market should continuously be one of the main directions attracting and stimulating Vietnam's production and exportation.

Table 2.

Contribution to GDP growth by expenditure category 2001-2012.

	2001	**2005**	**2008**	**2009**	**2010**	**2011**	**2012e**
GDP growth (percent points)	**8.98**	**8.44**	**6.2**	**5.32**	**6.8**	**5.89**	**5.03**
Final consumption	4.7	5.29	5.5	3.53	5.1	3.7	3.6
Gross capital formation	4.36	3.97	2.2	1.31	2.9	0.6	0.7
Net Export	*-0.02*	*-1.57*	*-1.9*	*1.66*	*-0.7*	*1.03*	*2.96*
Import	-4.51	-8.47	-9.6	-2.41	-9.2	-6.09	-4.27
Export	***4.49***	***6.9***	***7.7***	***-0.75***	***8.5***	***7.12***	***7.23***
Statistical Discrepancy	-0.06	0.75	0.4	-1.18	-0.5	0.56	-2.13
GDP (percent portion)	**100**	**100**	**100**	**100**	**100**	**100**	**100**
Final consumption	52.3	62.7	88.7	66.3	74.4	62.7	71.5
Gross capital formation	48.6	47.0	35.5	24.6	42.8	10.3	13.9
Net Export	*-0.2*	*-18.6*	*-30.6*	*31.2*	*-9.9*	*17.5*	*58.8*
Import	-50.1	100.3	-154.8	-45.1	-134.9	-103.5	84.9
Export	***49.9***	***81.7***	***124.2***	***-14.1***	***125***	***120.9***	***143.7***
Statistical Discrepancy	-0.7	8.9	6.5	-22.1	-7.3	9.66	-42.3

Sources: Computed by authors from statistics of GSO Vietnam.

The strong export performance of Vietnam for the years of 2001-2012 has greatly contributed to improve the trade balance and current accounts, stabilize macroeconomic and create some more extends in policy buffers for achieving social and environmental purposes. Exports continue to grow rapidly, enabling Vietnam to post a surplus on its trade account in 2012 for the first time since 1992. The improved trade and current account balances have helped the State Bank of Vietnam to shore up foreign exchange reserves—from 1.6 months of import cover at end 2011 to about 3 months in the third quarter of 2013.

Headline inflation has been falling in the last 24 months. In July 2013, headline inflation had fallen to 7.3%—largely attributed to the easing of food price and stabilization measures. Greater macroeconomic stability has helped Vietnam to regain the confidence of investors.

Empirical data also points out the significance of international trade in general in Vietnam's path towards its millennium goals. In particular, the sustainable export growth in the sectors of agriculture, forestry and fishery and labor-intensive manufactures as garments, textile, footwear and furniture… has actively contributed to the reduction and elimination of hunger and poverty, creation of new jobs for the abundant labor forces and improvement of their incomes. In addition, increasing earning from international trade would be redistributed into social and environmental funds that better serve the achievement of social and environmental protection goals. If this is not the case, Vietnam has to acquire more knowledge and awareness on the social and environmental dimensions of sustainable development through international trade exchange.

Main Challenges for the Sustainable Development of Vietnam's Current Export

As of now, Vietnam export growth is still solid in spite of the unfavorable circumstance of the global market post-crisis. Booming exports with sustained flow of external capital and remittances, and slower import growth have all helped Vietnam turn around its external balances. In 2012, Vietnam registered its record trade and current account surpluses. The trade balance (based on the balance-of payments definition) was estimated to yield a record surplus of 6.5% of GDP in 2012. Similarly, the current account balance has changed from a huge deficit of 11% of GDP in 2008 to a minor surplus of 0.2% of GDP in 2011 and a record surplus of about 5.9% in 2012. However, this performance may not last forever as imports are expected to pick up once the economy regains strength.

In international market, Vietnam export still has to face the sluggish global demand and the increase of protectionism on the import markets as a consequence of the great global financial crisis and economic recession in the year 2008-2009. Since 2010, the world economy has been recovering thanks to the financial and economic stimulus measures of governments. But the process of recovery is also encountering many difficulties and obstacles including depressed customer demand, heavy public debts, political instability, diseases, natural disasters and climate changes. In times of hardships, many governments have introduced new protectionist measures such as increases in tariffs and also non-tariff barriers, anti-dumping policies or trade-unfriendliness actions. Even some of the financial stimulus packages introduced to confront the crises contain elements which favour domestic goods and services at the expense of imports, etc. As Vietnam's economy is heavily dependent on exports, lower demand from major markets like US, EU, Japan and the emerging trade protectionism could damage Vietnam exports and ultimately slow down the growth of its economy.

The global economic recovery has become more apparent since the second half of 2013. Global growth momentum has accelerated during the second and third quarters of 2013, while many downside risks are marginal. The second quarter of 2013 marked the first time in 30 months that the economies of the Euro area, Japan, and the United States all posted positive growth. The Euro area escaped its recession in the second quarter, registering a growth rate of 1.2%. Recovery intensified in the United States, with its economy growing at 2.5%, while Japan's economy expanded by a solid 3.8%. Similarly, growth accelerated in several emerging markets including in Brazil, China, Malaysia, South Africa, and Turkey. Leading indicators of economic activities also suggest that global production and trade cycles may have bottomed out in the third quarter. Yet the risks to global recovery coming from the withdrawal of monetary stimulus from more advanced economies and an abrupt slowdown of investment in China, etc remain prominent. International conditions will continue to create new opportunities as well as challenges to the development in Vietnam export.

In the domestic market, the slow pace of structural reforms has led to an economic slowdown. Vietnam's economy is experiencing its longest period of modest growth since the beginning of economic reforms in the late 1980s. GDP growth slowed to 5.03% in 2012 from 6.0% in 2011 and 6.8% in 2010. Vietnam's economy is anticipated to grow at a moderate pace of around 5.3% during 2013.

Economic and export development of Vietnam currently has to face many challenges such as slower economic growth with weak domestic demand including investment and consumer demand, great bank bad debts, frozen housing market and difficulties of business sector. In particular, nearly 55,000 businesses are reported to have closed, liquidated, or temporarily suspended their operations during the first eleven months of 2013 - a 8.4% increase compared to the same period of 2012, while newly registered enterprises amounted to 71,000, achieving a rise of 9.5% in quantity but reduction of 15.4% in registered capital compared to the same period of 2012, and demand for credit has waned in light of weaker business prospects.

To combat these economic difficulties, Vietnam's government has introduced a number of measures to support GDP growth. The State Bank of Vietnam has aggressively cut interest rates in response to the slowdown in growth and falling inflation. The Ministry of Finance also introduced several fiscal measures including reductions in tax rates and tax payment delays to assist struggling enterprises. A series of initiatives were introduced by the Ministry of Planning and Investment and the Ministry of Industry and Trade to stimulate production and exportation, etc.

Despite these efforts of the government, the situation has yet to be significantly improved. The economic growth continues to slow and risk of stoking inflationary pressures and reverses the recent gains in macroeconomic stability. These difficulties can be attributed to inappropriate economic growth model. Vietnam has been in the factor-driven stage of development for quite a long time and is slowly transforming into efficient and innovation-driven one. Furthermore, the institution of market economy remains incomplete with the leading role belonging to state-owned enterprises, little accountability and transparency, strong influence of interest groups in policy making process and serious corruption, etc. Administrative procedures, especially in the fields of tax, customs clearances, business registration… remain complicated and unclear, along with lacking and backward infrastructure as well as low quality of human resources, have numerous negative impacts on Vietnam's economic and export growth.

Apart from the common difficulties of Vietnam's economy growth, Vietnam's export has to face many issues of its own. Notably, the export structure is still based mainly on primary and labor-intensive manufacturing products such as raw materials, agricultural, forestry and fishery products, textile and garment, footwear... High value added and technological-intensive products account for a very small portion of total export value. In manufacturing exports and global value chain, Vietnam has only participated in the assembling stage - the one with the lowest value added. The increasing share of FDI sector in the total exports of Vietnam may also impact sustainable export development of Vietnam, unless domestic enterprises should become stronger and more competitive. The service export will still lag far behind commodity exports, etc.

Policy Implications and Recommendations

For a stronger export performance in contribution to sustainable economic and social development of Vietnam, the following policy measures are recommended:

- aggressive efforts from government and society to speed up economic structural reform, with special focus on SOEs and banking sectors; and at the same time to take measures to maintain macroeconomic stability in order to strengthen confidence of investors and businessmen.
- rapid transformation of economic growth model from horizontal to intensive development with enhancement in efficiency and innovation
- aggressive efforts from government to improve business environment in order to strengthen the competitiveness of Vietnam through:
    - continuing improvement of tax policies for more transparent, simple yet concrete and easy applications.
    - committed compliance of international agreements.
    - accelerated reform of administrative procedures, especially those of customs clearance and fast application of electronic governing; strengthened capability of public administration; greater transparency and clarify of government’s mechanisms and policies; and constantly improved legal framework aiming at improving investment environment.
    - active measures to tackle corruption (at both national and local government): Strengthening anti-corruption efforts by giving the anti-corruption board more autonomy and resources; accelerating the deployment of the Grassroots Democracy Decrees, which decentralizes accountability and transparency to citizens within provinces, districts, and communes.
    - investment in the construction of infrastructure: ensuring stable power supply and convenient information as well as traffic networks; building and running high technology parks, I.T. parks, etc.
- an emphasis on human resource development:

- creativity in basic education: Adjusting the curriculum away from rote memorization to spur new ideas, encourage creativity, and applaud inventiveness early on during school years; considering inter-school competitions and awards for "Vietnam's most creative student."
- public/private partnership for funding of R&D and training. Vietnam is currently far from the technological frontier in terms of innovation, R&D and innovative activity. Therefore, the enhancements in public/private partnership for funding of R&D and training should be an effective solution for human resource development.

- incentives for priority activities that move up the value chain (i.e., tax credits for R&D, accelerated depreciation, etc).
- change in equitization of SOEs into privatization: Engaging in complete, gradual privatization, using the State Capital Investment Corporation as the vehicle; empowering private firms to form independent business associations...
- priorities and incentives to develop the supporting industries: introducing aggressive FDI promotion policies to develop parts and components sectors; improving the capacity of essential processing industries such as piercing metal details, casting, plating and template manufacture under the framework of the national program on development of supporting industries; accelerating the reform of state enterprises engaged in mechanical engineering, plastics and casting to become enterprises specialized in manufacturing products for supporting industries, etc

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