



Vietnam—a pause in its expansion?

Vietnam in brief

Vietnam is a very different country from India. It is geographically tiny in comparison and its population is only about 8% of India's. In the last 30 years it has also had to recover from the ravages of war, the loss of financial support from the old Soviet Bloc and the rigidities of a centrally planned economy. Substantial progress was made during the 1990s with growth averaging 9%. The 1997 Asian financial crisis highlighted the problems in the Vietnamese economy and temporarily allowed opponents of reform to slow progress towards a market-oriented economy. GDP growth fell to around 6.8% per year from 1997 up to 2005, when it hit 8%.

Membership of the ASEAN Free Trade Area (AFTA) and the US-Vietnam Bilateral Trade Agreement in December 2001 have led to even more rapid changes in Vietnam's trade and economic regime. Vietnam also hopes to become a member of the World Trade Organization (WTO) this year, which would allow it take advantage of the phasing out of the Agreement on Textiles and Clothing, which eliminated quotas on textiles and clothing for WTO partners on January 1, 2005.

The footwear industry in South East Asia has expanded dramatically in recent years and made a significant contribution to industrial growth in many of its

countries. Vietnam in particular has developed at a tremendous rate since 2000 to the extent that, after China, it has become the second most feared competitor for the remainder of the world's footwear producers. How has this come about?

Looking at this short time scale, by the end of 2003, more than 750 complete production lines had been installed with the capability to produce various types of finished shoes with a total annual capacity of 520 million pairs. That is serious investment. Most of these new companies have built up a stable relationship with foreign partners and customers aimed at maximising production capacity.

More than 380 companies throughout the country are involved in producing finished leather, footwear and components. Of these, only 55 are state-owned, 177 are private companies, 134 are Foreign Direct Investment (FDI) and 14 are joint ventures. Between them, they employ almost 500,000 people directly, with a corresponding number working in related support industries and services.

This marked a major but realistic change in government policy. It saw that, in order to take advantage of an industry that could quickly create this degree of employment in a predominantly agrarian economy, it had to attract outside investment and expertise. State control was not the answer and taking its cue

National statistics*

Population	84.4 million (2006 est.)
GDP	\$43.75 billion
GDP per capita	\$2800
GDP growth	8.4%
Inflation	8.4%
Budget deficit	3% of GDP
Current account	-4% of GDP
External debt	43.8% of GDP
Exports	\$32.23
Imports	\$36.88
Deficit	\$4.65

*2005 estimates

from China, Vietnam changed direction.

A further sign of the government's support for the leather and footwear industry has come in the latest review of import taxes. The Ministry of Finance has announced that certain goods sectors have been awarded preferential tax tariffs under the ASEAN China Free Trade Agreement (ACFTA). Providing products are imported from ACFTA countries directly to Vietnam, a zero tax rate will apply. This includes dyes and leather tanning products. High tax rates will remain on other sectors such as textiles and garments, where the rate will be 30-35%.

The domestic market

Vietnam is also very different to India with regard to its domestic market. While



Stitching bootie uppers. Courtesy Haksan Limited

it is also fragmented, with many small retailers, it does not have the large proportion of artisans able to supply the small quantities they need. Vietnam's footwear manufacturers have gone in one quantum leap from nothing to either medium or large mechanised operations, making it difficult to supply such small customers at a profit. The result has been a marked reluctance to supply the domestic market by factories that export over 90% of a total production that is fast approaching 500 million pairs of shoes per year.

At the same time, its people need shoes and this hole has been filled by imports from China and Taiwan. These two provide the bulk of the three million pairs Vietnam imports per year in the form of a wide range of relatively cheap footwear. Demand, however, is growing in line with increasing disposable income and it is thought that total annual domestic consumption is approaching 160 million pairs, based on each consumer needing two pairs. The fact that Vietnamese exporters are now facing tougher competition due to rising costs and protective trade barriers may cause them to take more interest in the local market.

Indeed, there are changes occurring that may encourage them further. Local quality standards are lower than on export markets and there is no domination by large branded buyers. More flexible production planning would take out many of the small volume problems. Increasing demand and with improvements in logistics, Vietnam is becoming a far more attractive footwear

market for local manufacturers. Proof of this lies in the fact that whilst imports remained steady at an estimated 1.6 million pairs between 2000 and 2002, they fell 12.5% in 2003 and were predicted to be a further 28.5% down in 2004.

Imports (million pairs)				
2000	2001	2002	2003	2004
1.6*	1.6*	1.6*	1.4*	1.0*

*Estimate

Vietnam's footwear exports

In 2003, the last year for which accurate figures can be quoted, Vietnam produced 416.6 million pairs of which it exported 393 million to the value of \$2.267 billion, raising the industry to third place after crude oil, textiles and garments. It represents 11% of the country's exports in dollar terms.



Assembly line. Courtesy Haksan Limited

Exports (\$ billion)

1999	2000	2001	2002	2003
1.33	1.47	1.58	1.85	2.27

Exports (million pairs)

2000	2001	2002	2003	2004
276.6	*291.8	333.0	393.0	420.2

*Estimate

The key export market is the EU which accounts for 70.6% of the total and is way ahead of the USA at 12.5%, Japan with 2.7% and other countries that take the remaining 14.2%. Estimates for 2005 suggest that the export value of footwear is set to rise to \$3.1 billion and to double to \$6.2 billion by 2010. This again demonstrates the Vietnamese government's intention to throw its weight behind investment and further development of this important foreign currency earner. It also explains why it has reacted so bitterly over the recent introduction of EU tariffs.

Production breakdown (million pairs)

Category	2003	2004
Sports	234.0	
Textile	28.6	
Women's	82.4	
Other	70.6	
Total	416.6	*445.2

*Estimate

Vietnam is now the fourth largest producer of footwear in the world after China, India and Brazil. It has traditionally exported most its footwear output to Europe, but since the opening of the US market to Vietnamese manufactured products, exports to that country are growing rapidly. ➤

**Top six footwear export markets
(2004 - million pairs)**

Germany	83.4
UK	82.0
France	45.8
USA	43.7
Italy	21.3
Spain	16.4

State of the industry

The biggest problem facing the footwear industry in Vietnam is the lack of locally produced raw materials, particularly leather. Here it is the complete opposite of India. While so many shoes are at the cheaper end or use textiles and synthetics, it is not too serious. But, if the industry wants to break away from producing cheap sports shoes on a contract basis for large overseas buyers, it will have to upgrade in terms of quality and styling. This will inevitably also increase its need for

quality leathers at world prices. The only advantage it will then have will be in terms of labour costs and these will also rise in just the same way as they are in China.

The second factor is that of anti-dumping duties. While the EU provisionally hit China with a 19.4% tariff on leather shoes, it also slapped 16.8% on Vietnam. Whilst China is regarded by all other footwear manufacturing countries as the major threat to their production, it is one they can do little about such is the sheer scale of the Chinese industry. Vietnam is perceived to be weaker and more vulnerable. While the tariffs do not affect high-tech sports shoes, it hits the very products—leather shoes—that Vietnam needs to produce more of if it is to raise its export profile. It is therefore caught between the rock of imported leather and the hard place of anti-dumping tariffs.

The fact that the Vietnamese government places such strategic importance on its footwear industry is a further grievance for foreigners who have used it to support their claims that the dumping they allege has taken place has government blessing. Whether these tariffs will stay in place long-term is debatable. Markus Cornaro, head of the EU Commission in Vietnam, declared in May that the 16.8% duty rate on leather shoes was a temporary solution and that the Commission was considering a final decision based on the interests of the relevant parties.

Whatever the outcome of this trade row it will not be immediate and, in the meantime, a brake has been put on Vietnam's meteoric rise. Its declared intention of hitting the \$6 billion mark to put itself into second place behind China in world ratings will not be as easy to achieve as it first thought.

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