# Non-Equity Modes of Trade in ASEAN

## Promoting new forms of trade between Japan and ASEAN

PAPER 10

DECEMBER 2018

ASEAN


ASEAN-JAPAN CENTRE

国際機関 日本アセアンセンター

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The following symbols have been used in the tables:

- Two dots (..) indicate that data are not available or are not separately reported.
- A dash (-) indicates that the item is equal to zero or its value is negligible.
- Use of a dash (-) between dates representing years, e.g., 2015–2016, signifies the full period involved, including the beginning and end years.

Reference to "dollars" ($) means United States dollars, unless otherwise indicated.

There are 10 papers in total. The other nine papers will be produced subsequently.

Paper 1. Brunei Darussalam
Paper 2. Cambodia
Paper 3. Indonesia
Paper 4. Lao People's Democratic Republic
Paper 5. Malaysia
Paper 6. Myanmar
Paper 7. Philippines
Paper 8. Singapore
Paper 9. Thailand
**Paper 10. Viet Nam**

Prepared by Dr. Shunji Karikomi (Viet Nam Research Institute, Waseda University, Japan) and trade staff members of the AJC under the direction of Masataka Fujita (AJC). Errors and omissions are only those of the authors and should not be attributed to their respective organizations.

# CONTENTS

# KEY MESSAGES

- From being one of the world's poorest countries Viet Nam has become one of the most dynamic manufacturing countries in ASEAN. With a relatively young population and average annual GDP growth rates of 6.4 per cent since 2000, the country's prospects for economic development are bright, in both the short and the long term.
- The volume of non-equity mode (NEM) exports from Viet Nam has been increasing, reaching an estimated $62 billion in the goods sector alone in 2016. NEMs are estimated to have accounted for 35 per cent of total merchandise exports in 2016. If services are included, NEM exports that year would have reached at least $70 billion.
- The textile and apparel industry has traditionally flourished in Viet Nam. The export value of textile and garment products in 2016 was $23.8 billion, with 10 per cent average annual growth in 2014–2016. Viet Nam is the fourth largest garment exporter, following China, India and Bangladesh. Textile and garment exports under NEMs or subcontract manufacturing are estimated at $20 billion, approximately 11 per cent of all merchandise exports.
- The electronics industry accounted for 23 per cent of Vietnamese GDP in 2016. Viet Nam's electronics industry is the twelfth largest exporter in the world and the third largest in ASEAN. However, leading electronics manufacturers still import the majority of the parts and materials required for products that are assembled in Viet Nam facilities. Local vendors are capable of producing only low value added products such as basic plastic components, packaging and instruction manuals.
- Product assembly businesses (including electronics) and garment businesses have flocked to Viet Nam. These two rapidly expanding industries require components and raw materials that cannot be procured in the country, the greatest amount of which has thus been imported. In order to promote NEM production in these industries, it is necessary to nurture supporting industries.
- IT-BPO (information technology and business process outsourcing) is the leading growth industry in Viet Nam, with $4.6 billion in sales in 2016. It is set to grow faster in the near future, as Viet Nam has become better known as an outsourcing destination. However, the lack of education and training in IT, and the lack of practical application and soft skills are obstacles to expanding the scale of the industry.
- Viet Nam's retail industry is forecast to reach a value of $109 billion in 2017. Attracted by low barriers to trade, many international retail groups have entered the local market, which has nearly 100 million consumers. International retailers are expanding their stores by franchising. In this industry, transnational corporations (TNCs) and local partners can work together through international brands and sales networks to optimize each other's resources.
- Facilitating and promoting NEMs requires an enabling legal framework, stronger promotion policies and home-country support. Viet Nam is still an emerging country with obstacles that can negatively affect local business operations. The government needs to relax rigid regulations and to simplify various business procedures.
- Viet Nam's current educational and vocational training systems do not produce an adequate level of skills in its entire workforce. Under the ASEAN Economic Community, Viet Nam will have to open its doors to skilled labour from other ASEAN members in certain sectors. Vietnamese workers cannot continue to compete with others in the region unless their professional qualifications, foreign languages and soft skills improve further.

- Development strategies related to NEMs can be realized. It is important for Viet Nam to implement policies for productive capacity-building, including education policy. Technological policies are needed to encourage the development of local firms and to overcome the low value added of activities under NEMs.
- For TNCs, NEMs can be used as test cases before undertaking full-scale entry into the market. Viet Nam will need to maintain its competitiveness by improving the production capacity of local firms so that foreign clients will not choose to withdraw readily if the test case does not work out.

# 1. INTRODUCTION

The international business conducted by transnational corporations (TNCs) has traditionally been trade and investment. It is especially common for TNCs to engage in foreign direct investment (FDI) when manufacturing overseas in order to take advantage of wage disparities, government support or other benefits.

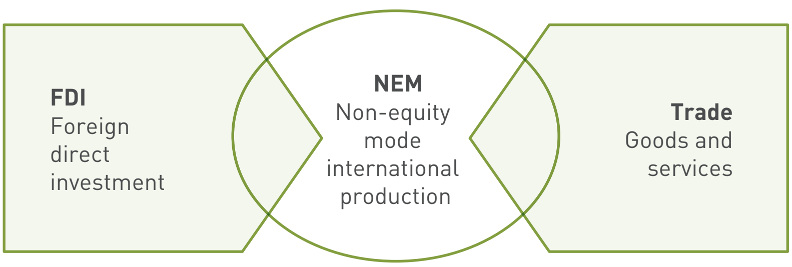
However, as TNCs' business networks grow larger and more diverse, TNCs have come to maintain core competencies that generate large amounts of value while outsourcing some production processes that create lower value. Value chains, which encompass all stages from production to sales, are being shaped at a global level, and by controlling and managing them, TNCs can control their resources and market efficiently.

Even if TNCs do not engage in equity participation (investment), non-equity modes (NEMs) of international production are still carried out by partner companies managed by TNCs. One typical format is contract manufacturing. In the past, processing on consignment has been used in developing countries to perform labour-intensive operations, such as those involved in manufacturing clothing, shoes and toys, but the scope of NEM has expanded to include electronics manufacturing services (EMSs) and information technology and business process outsourcing (IT-BPO) services. Other NEMs include contract farming, franchising, licensing and management contracts.

As economies grow more globalized, it is not sufficient to look only at FDI when considering how, and to what degree, TNCs can control global value chains (GVCs). For example, China is now one of the world's largest foreign-investing countries, but the involvement of Chinese companies in GVCs is still in low-end stages. Even when TNCs do not use FDI, they use GVCs and industrial distribution to control important stages of creating high value added products. Recently, international GVCs have been formed through the intertwining of FDI, trade and NEMs. NEMs are modes positioned midway between FDI and international trade (figure 1), and cover a wide range of scales and scopes.

In 2016 Viet Nam was the forty-seventh largest economy in the world and the sixth largest economy in ASEAN in terms of GDP. The country began developing economically with the Doi Moi policy, initiated in 1986, which promoted shifting to a market economy and opening up to foreign business. In the 1990s, the economy developed through infrastructure investment and FDI. In this period, Viet Nam's GDP grew an average of 7.5 per cent a year. Under the impact of the Asian currency crisis, however, Viet Nam's economy slowed and faced a decrease in FDI. In the mid-2000s, rising wages in Chinese

Figure 1. **Positioning of selected types of cross-border NEMs**




Source: UNCTAD (2011).

coastal areas and the manifestation of the risks of doing business in China brought increased attention to Viet Nam as a possible additional candidate or as an alternative to China. After the late 2000s, the country again attracted attention as an investment location for foreign firms. Its economic growth accelerated because of many factors, including a shift in production from China in light of both the "China Plus One" strategy and Viet Nam's joining the World Trade Organization (WTO) in 2007.

The GDP annual growth rate of Viet Nam in 2016 was 6.2 per cent, and it had been at a 6 per cent level since 2011, excluding 2012 and 2013. Among major factors behind the high growth during the 2010s were increases in production and exports due to business advancements by foreign companies into the country that led to employment growth and income increases. Now Viet Nam is a middle-income country, with a GDP per capita of $2,088 (2016), though that is still lower than the ratios in Indonesia ($3,362) and the Philippines ($2,858).

With the recent economic growth, NEM trade is spreading in Viet Nam in several forms: international subcontracting in manufacturing industries, such as electronics and garments; contract farming in agriculture and fishery; international franchising in fast food and retail stores; variations of build-own-operate transfer arrangements and other concessions in infrastructure projects; and management contracts (e.g. in international hotel chains) (table 1). Offshore software development (i.e. IT-BPO) has become popular in Viet Nam, and these businesses are largely undertaken under contractual agreements with foreign entities. This paper examines the case of Viet Nam in the overall framework of the ASEAN-Japan Centre (AJC) project (box 1), particularly in four industries: garments, electronics, IT-BPO and retail trade.

Box 1. **The NEM project by the ASEAN-Japan Centre**

Other than arms-length relationships, equity-holding is not the only means of exerting control over global value chains (GVCs). Companies also enter into contractual relationships with other independent firms. Such trade is gaining importance as the system of global production becomes more integrated and value chains form. This is an area in which lack of knowledge and a huge gap of research exist in ASEAN. It calls for an overall analytical framework to assess development impacts in order to propose a generic policy framework for dealing with these kinds of transactions.

The fundamental difference from normal trade is that non-equity forms of operations relate to a contractual partnership between private parties. The role of the state in relation to this partnership is limited to setting the framework conditions within which the private parties can freely negotiate the terms of their cooperation. By understanding this phenomenon better, including its scale and scope, and filling in a policy analysis gap, the ASEAN–Japan Centre (AJC) can provide ASEAN country governments with policies to consider in order to fully benefit from these new forms of trade, as well as from investment.

In order to understand the scale and scope of non-equity involvement in major industrial sectors, a case study methodology is used. The reasons for taking this approach are two-fold: (1) balance-of-payments and supplementary statistics do not provide the detail necessary to accurately measure cross-border non-equity participation, and (2) the relevant microdata are fragmented and disconnected. As much as possible, each case study builds on existing research and statistics.

New opportunities are opening up for ASEAN countries the international innovation networks of transnational corporations (TNCs). Although attracting FDI and encouraging foreign TNCs to establish affiliates remain important options for ASEAN countries, governments also need to review current regulatory regimes in the context of international innovation networks. A key objective of this study is to make recommendations on which policies (investment and industrial) governments need to consider in order to fully benefit from emerging opportunities.

Table 1. **Selected NEMs in Viet Nam, with examples of typical industries and companies**

| Modality | Description (in the international context) | Typical industries | Company examples |
|---|---|---|---|
| Subcontracting | Agreement whereby a TNC contracts out to a host-country firm one or more aspects of product design, processing or manufacturing. Includes contract manufacturing and design, and outsourcing in the case of services or business processes. | Electronics | ASTI Electronics |
| | | Garments | AGV |
| | | Automotive | NGK |
| | | IT | EVOLABLE Asia<br>Vitalify Asia |
| Contract farming and/or contract mining | Agreement between a TNC buyer and host-country farmers and/or miners (including governments), which establishes conditions for the production and marketing of farm and/or mining products. | Agriculture | CCL Products |
| | | Fishery | CP Group |
| Licensing | Contractual relationship in which a TNC (licensor) grants to a host-country firm (licensee) the right to use an intellectual property (e.g. copyrights, trademarks, patents, industrial design rights, trade secrets) in exchange for a payment (royalty). Includes brand licensing, product licensing and process licensing. (Also called cross-licensing and intrafirm licensing.) | Food | Chikaranomoto |
| | | IT-BPO | Qualcomm<br>(PCB Graph Tech) |
| | | Pharmaceutical | Innovus<br>(Densmore) |
| Franchising | Contractual relationship in which a TNC (franchisor) permits a host-country firm (franchisee) to run a specified business modelled on a system developed by the franchisor in exchange for a fee. | Retail | FamilyMart/JUMBO |
| | | Education | Cohas Kids |
| Management contracts | Agreement under which operational control of an asset in a host country is vested in a TNC contractor that manages the asset in return for a fee. | Tourism and hospitality | Regent Hotel (BIM), Hilton (BRG) |
| Other e.g. build-operate-transfer (BOT) and the like | Includes concessions, lease agreements, BOT arrangements, etc., in the context of public–private partnerships. | Infrastructure | JEXWAY, NPC EVN |

Source: AJC.

# 2. CHARACTERISTICS OF NON-EQUITY MODALITIES IN VIET NAM

## 2.1 Scale and scope

Table 1 describes various forms of NEMs in use in Viet Nam. NEMs can be compared with FDI from the perspective of TNC motivation. For example, contract farming is motivated by a search for product resources. Contract manufacturing, outsourcing and subcontracting are motivated by the desire to improve efficiency by reducing costs. Licensing and franchising are motivated by the desire to capture markets. Whereas subcontracting is similar to FDI in that it consists of transferring resources, technologies and expertise to contractors operating locally, licensing and management contracts involve little transfer. Following is an overview of the features of each NEM in Viet Nam.

### (1) Manufacturing: Subcontracting

Subcontract manufacturing grew significantly in the electronics industry in the 1990s worldwide. During the preceding decades, major electronics companies dedicated themselves to research and development (R&D), product design and brand management, and had EMSs (e.g. Celestica, Flextronics and Foxconn) perform manufacturing on assignment. A small number of contract manufacturers control the industry: the top 10 account for two thirds of global EMS sales. Of these, seven are headquartered in East Asia.

The electronics and electrical industry thus has been playing a major role in driving Viet Nam's exports as well as FDI into the country. As the top dollar earner of the country in 2016, the industry accounted for 30 per cent of total exports, at $53.2 billion. Telephones and parts are the most exported items, accounting for about 19 per cent of all exports from the country. Since Samsung Electronics built its mobile-phone-related factories in 2009, mobile phones and parts have become the largest export goods of Viet Nam, overtaking garment products in 2013.

Samsung Electronics, Intel, Nokia, LG Electronics and other global companies have made Viet Nam a centre of global smartphone production. Foreign firms export about 80 per cent of total production. As of 2016, there were 115 registered companies in the industry, the majority of them companies from Japan, the Republic of Korea and the United States. Vietnamese subcontractors provide parts for those foreign electronics manufacturers.

Garment manufacturing is an important industry for less developed countries, as it establishes a foothold for industrialization. Labour-intensive production processes are a good fit for developing countries with low-cost labour forces. Many foreign textile companies have therefore moved into Viet Nam in order to take advantage of its low labour costs. These companies include Japanese companies such as Wacoal, Gunze and Itochu, and American ones such as Gap, as well as numerous textile companies from countries such as China, the Republic of South Korea and Taiwan Province of China. In addition to textile companies, U.S. footwear companies such as Nike are also moving into Viet Nam.[1]

[1] A high number of foreign textile companies have entered the Vietnamese market because of the low labour costs and because of the U.S. and Vietnamese participation in the Trans-Pacific Partnership (TPP) negotiations since 2010. Roughly half of Viet Nam's textile products are exported to the United States. Once the TPP took effect, there was expectation that the export destination of textile products from Viet Nam base would expand to TPP signatory countries. However, because the United States has pulled out of the TPP, Viet Nam's competitive position with respect to tariffs on exports to that country will not be realized.

The textile and garment industries have played important roles for economic development in Viet Nam and have been growing constantly. Over 7,000 textile and garment companies operate in the country, and the industry employs more than 3 million workers. The export value of textile and garment products in 2016 was $23.8 billion, having grown 10 per cent per year on average in 2014–2016. Viet Nam is the fourth largest garment exporter in the world, following China, India and Bangladesh. Textile and garment exports through NEM or subcontract manufacturing are estimated at $20 billion, approximately 11 per cent of total merchandise exports. Local companies are involved directly in subcontracting for foreign apparel makers, including major brands such as Gap (Hansae Viet Nam) and Uniqlo (Viet Tien Garment).

### (2) IT-BPO: Outsourcing

In TNCs' value chains, in addition to the manufacturing process itself, business functional segmentation is also outsourced as a back-office function or a part of customer service. Major advances in information and communication technology (ICT) have made it possible to outsource, so that the locations where services are created are physically separated from the locations where those services are consumed. Service outsourcing began in developed countries in the 1990s with IT "onshoring," but in a short while shifted to developing countries where costs could be kept down. Information system companies are able to offshore, thereby actively using outside resources in implementing their business strategies. This is the result of economic globalization and regulatory relaxation, which has led to demand for greater cost reductions and higher quality levels in IT-related companies.

IT-BPO is one of the most dynamic industries in Viet Nam in terms of employment and revenues, generating $67 billion[2] in 2016. The local industry has attracted TNCs such as Fujinet, Harvey Nash Viet Nam and the Hoa Sao Group to operate in Viet Nam and has been helping create job opportunities in the sector.

Major outsourcing services contractors are primarily located in Asia. India, the Philippines and China enjoy advantages in terms of specific languages, IT skills, human resources and infrastructure. However, with mature outsourced operations in India and China, outsourcing locations have been expanding into other countries rapidly. Viet Nam has emerged as one of these new locations, with an outsourcing export value of $4.6 billion (table 2).

### (3) Agriculture: Contract farming

Contract farming is widespread. TNCs use this NEM in over 110 developing countries and it is involved in a diverse range of agricultural products (UNCTAD 2011). For example, in Viet Nam roughly 90 per cent of cotton and fresh milk, 50 per cent of black tea and 40 per cent of rice are sourced through contract farming (UNCTAD 2011). It is a tool for efficient procurement of agricultural products because it enables TNCs to secure the quantity and quality they require. In addition, farmers can secure stable sales and income levels. TNCs demand high quality from contract farmers, and farmers try to meet that demand. In return, farmers acquire new information and technology through contracts with TNCs.

Contract farming contributes to a large number of jobs for small-scale farms, generating a reasonable impact on the reduction of poverty. Although the total number of contract farms is hard to identify, data from individual projects show that several tens of thousands of workers are employed at farms that use this NEM.

[2] The figure includes hardware production.

### (4) Retail, Hotels, and Other Businesses: Franchising or management contract

Franchising is a well-known method of marketing and distributing products or services. In franchise agreements, typically franchisors provide franchisees with various types of support related to operation of the business. It can include initial and ongoing assistance, training, management guidance, marketing and human resource development. Through their franchise management, franchisors can not only expand operations rapidly and efficiently, but also procure capital. The method is being applied to the retail industry, including high street retail and goods stores, as well as to restaurants, hotels, business services, education and a variety of other business types.

Convenience stores and fast food chains have entered the Vietnamese market under franchise agreements with local partners. Viet Nam's retail market is characterized as one of the most dynamic in the region, with high annual growth rates. In 2016 Hanoi and Ho Chi Minh City were ranked among the top 10 Asian cities for retail expansion.[3] Convenience stores are proliferating rapidly in urban areas, replacing local shops and stores. The number of convenience stores owned by foreign companies, especially Japanese ones, is increasing rapidly. There has been an opening rush in the south, especially in Ho Chi Minh City, where there were 122 FamilyMarts (of 133 total) and 71 MiniStops as of February 2017. Other foreign-owned chains such as Shop&Go (Singapore) and Circle K (United States) have been entering the country since 2000.

Hotels are frequently operated as franchised businesses, with the franchisee taking on the style and brand reputation of a leading chain under license. Many structures are available for the ownership and operation of a hotel. The structure chosen depends on the scale of investment by the investor or hotelier, and land ownership is also an important factor. If the hotelier would rather minimize the obligations and responsibilities that are associated with land ownership, then a management contract is a good choice. International hotel chains such as Hilton and Sofitel are doing business in Viet Nam, through management contracts with local operators. Normally, the management contract lasts 10 to 20 years. The management fees charged by the operator in exchange for performing duties specified in the contract are the base management fee, calculated as a percentage of the hotel's gross operating revenue, and the incentive management fee, which is linked to the operating profit.[4]

• • •

NEM export activity in Viet Nam was estimated at $62 billion in the goods sector alone in 2016, with total exports of goods at $177 billion.[5] Services exports that year rose to $12 billion, from $4 billion in 2005, with average annual growth of 10.5 per cent during the period. As the travel service industry has continued to expand significantly, NEM activity in the industry has also grown. In fact, if services trade were considered, NEM exports of goods and services would reach at least $70 billion.

Table 2 presents a summary of NEM operations in the three major sectors for 2016. In each sector, NEM exports were substantial. In the primary sector, coffee production and exports under contract farming were operated and managed by companies such as CCL Products Group (Ngon Coffee)

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3 CBRE, Asia Pacific Research Reports 2017.

4 HVS (2014), Hotel management contract survey.

5 UNCTAD (2011) estimated global NEM production at more than $2 trillion of sales in 2010. Contract manufacturing and services outsourcing accounted for $1.1–1.3 trillion, franchising $330–350 billion, licensing $340–360 billion, and management contracts about $100 billion (UNCTAD 2011). However, the report also states that the analysis of NEMs is complex, as "the web of directly owned, partially owned, contract-based and arm's-length forms of international operation of TNCs is tangled, and some of the distinctions between the different modes are blurred". Thus, the analysis is limited to a number of industries in which NEMs are especially important.

Table 2. **NEM operations in the three major sectors, 2016**

| Sector | Primary | | Secondary | | Tertiary | |
|---|---|---|---|---|---|---|
| Industry (representative example) | Coffee | Shrimp | Garments and textiles | Electronics | Convenience stores | IT-BPO |
| Product or services | Green coffee bean (Robusta coffee) | Black tiger prawn; whiteleg shrimp | Apparel | Mobile telephone; computing | Small retail groceries; snack foods; confectionery; soft drinks; tobacco | Call centres; software development |
| Number of companies (NEM-related, estimation) | Over 100 (Viet Nam Cocoa Association: VICOFA) | 87 (Viet Nam Association of Seafood Exporters and Producers: VASEP) | Over 7,000 (Viet Nam Textile & Apparel Association: VITAS) | 115 (Viet Nam Electronic Industries Association: VEIA) | 1,561[a] | Over 1,000 |
| Major companies (TNC partners) | CCL Products Group (Ngon Coffee)<br>Olam International (Café Outspan) | Minh Phu Seafood Corp (Mitsui) | Hansae Viet Nam (Gap)<br>Viet Tien Garment (UNIQLO) | Four P Company (LG) | VinMart +; Circle K; B's Mart; FamilyMart; MiniStop; Shop&Go | Hoa Sao Group (Bellsystem 24)<br>Transcosmos<br>KDDI |
| Estimated export volume (Estimated exports by NEMs) | $3.3 billion and 1.75 million tons ($1.1 billion and 0.6 million ton) | $4 billion and 727,743 tons (2015) ($2.4 billion) | $23.8 billion ($20.0 billion) | $40.4 billion ($12.1 billion) | $205.0 million sales (2015) | $67.0 billion[b] sales ($4.6 billion) |
| NEM mode | Contract farming | | Subcontracting | | Franchising, licensing | Subcontracting |
| Estimated employment | 596,000 (global coffee platform) | Over 4 million in the fishery industry | 3 million | 8 million in the manufacturing industry | 15,000 | 780,929 |
| Average export growth | 10.3% average export growth over 2014–2016 | 3.5% average export growth in marine products | 10% average export growth over 2014–2016 | 29% average export growth over 2012–2015 | 293% sales increase from 2011(2015) | More than 10-fold sales growth over 2009–2016 |
| Market or trade scale | Germany 15.4%<br>United States 13.2% | United States 22.5%<br>EU 19.1%<br>Japan 19%<br>China 13.8% | United States 55%<br>EU 17%<br>Japan 14% (2015) | Smartphone-related products are the main export products | VinMart+ 60%<br>Circle K 13%<br>B's Mart 10%<br>FamilyMart 9%<br>MiniStop 5%<br>Shop&Go 3% | Japan<br>United States<br>EU |
| Product or service scope | By 2020, the goal is to process 25% of coffee domestically and produce 250,000 tons of instant coffee a year. | Viet Nam aims to reach the goal of $10 billion in shrimp exports. | All the stocks of Vinatech held by the Vietnamese government (53.5%) will be sold in 2018. | Korean companies lead local production and exports; 22.7% of export volume comes from Samsung Electronics. | Seven Eleven opened the first store in June 2017 in Ho Chi Minh City. It aims to open 100 outlets in Viet Nam by 2020. | Further human resource development is needed to meet the demand for IT engineers both domestically and abroad. |

Source: AJC.
Note: Selected industries only; 2016 data unless otherwise noted.
[a] As of 2017 February.
[b] Including hardware.

and Olam International (Café Outspan). Coffee exports produced through NEMs were estimated at $1.1 billion and 0.6 million tons in 2016, one third of the total exports in both value and volume. Most of this production went to Germany and the United States. Farmed shrimp is one of the major foreign currency earners in Viet Nam. Exports of farmed shrimp from Viet Nam in 2015 amounted to $4 billion and 727,743 tons, the largest volume in the world. The export destination was mainly Japan, but exports for the United States and the European Union (EU) have increased significantly.

The Vietnamese government aims to attract not only FDI by TNCs, but also NEMs for production for international distribution. NEMs in all sectors have been contributing to the economic development of the country.

## 2.2 NEMs by modality

Many foreign firms and TNCs do business with local partners in the form of NEMs in various industries. The ways they are involved in NEMs and their contributions to the national economy vary by modality and industry. This section examines modalities such as subcontracting and franchising by looking at particular industries that rely on them.

### (1) Subcontracting: Textile and garment manufacture

Subcontracting is a method of production and processing in which an outside company or provider is hired to perform specific parts of a business contract or project. In the past, Japanese companies have subcontracted with companies in China, which is nearby and has low labour costs. However, as labour costs there rise, subcontracting (also called processing on consignment) is shifting to the countries of Southeast Asia. Viet Nam is one country that is drawing a great deal of attention. This is because in addition to its low labour costs, it also has increasingly developed infrastructure, which makes easy to carry out production on consignment in various types of industries. The general flow of how a TNC outsources the manufacturing process in Viet Nam appears in figure 2.

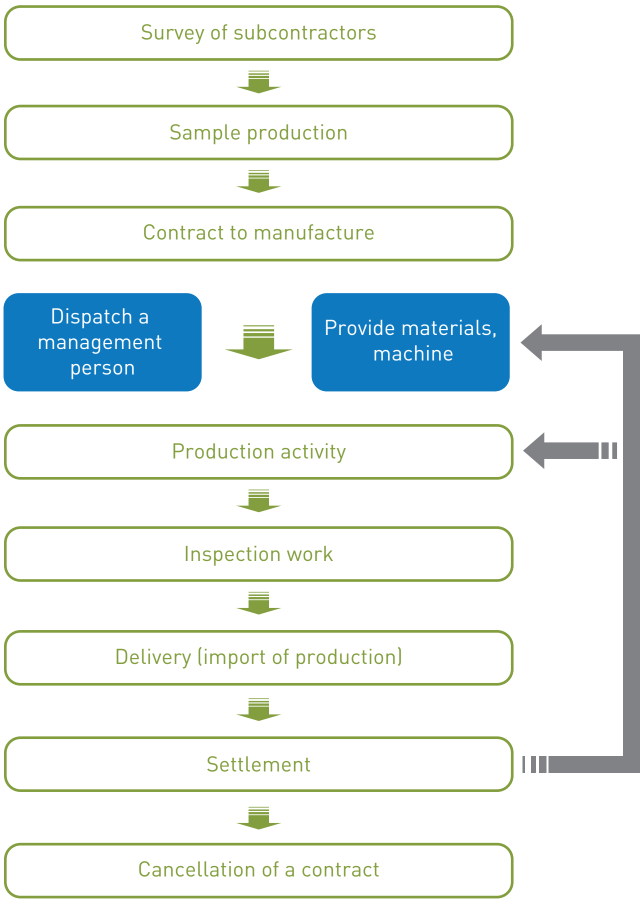
Sewing is the most labour-intensive processing stage in the garment industry and has the lowest rate of return. Sewing is the stage that newcomers to the industry often choose to enter first because it does not require high investment in technology. Countries with developed apparel industries, having participated in GVCs for a long time, no longer perform steps in this stage but tend to outsource them to developing countries such as Viet Nam, Cambodia and Bangladesh, countries that have cheap labour and underdeveloped production of input materials. This is a common feature of the production stage in the apparel industry around the world.

For enterprises engaged in such processing, value added earned in the apparel segment will also vary depending on export mode; for example, "cut, make, and trim" (CMT) products (for details, see box 2). CMT processing on consignment refers to garment manufacturers handling the three processes of cutting, making, and trimming in production and distribution networks. It is the main form of production and distribution in Viet Nam.

Viet Nam has several powerful garment manufacturers, but even these companies do not make their own plans or their own brand or design decisions, or handle distribution or market formation. As for original equipment manufacturing (OEM) production, almost no companies perform material selection and procurement on their own. In many cases, companies are merely involved in producing and stocking materials designated by the buyer.

For raw material procurement garment manufacturers rely on imports from other economies such as China, Taiwan Province of China and the Republic of Korea (figure 2). In fact, many Japanese garment firms in Viet Nam entrust only the sewing process to local companies. Suppliers of raw

Figure 2. **Flowchart of contract manufacturing**




Source: AJC.

materials and fabrics are located in China, sewing is done in Viet Nam and finished products are then exported to Japan. Many garment manufacturers intend to increase their procurement from Viet Nam in the future, but in the current OEM scheme, they cannot find suppliers there.

Box 2. **Outsourcing apparel businesses for garment export**

Apparel businesses that subcontract for garment exports typically apply one of four modes of export: CMT, OEM, ODM and OBM.

**1) CMT (Cut, Make, Trim)**

This is the easiest export method in the apparel industry and brings the lowest value added. Under this method, TNCs offer all the inputs for production including raw materials, transportation, designs and specific requirements; manufacturers carry out only the stages of cutting, sewing and trimming the products. Businesses working under this export method need only a basic understanding of design patterns and the ability to produce finished products.

.../

Box 2. **Outsourcing apparel businesses for garment export** (Concluded)

**2) OEM (Original Equipment Manufacturing)**
This export method, which entails buying raw materials and producing and selling final products, creates higher value added than CMT. Unlike under CMT, local firms buy necessary material inputs instead of being supplied with them directly by their buyers.

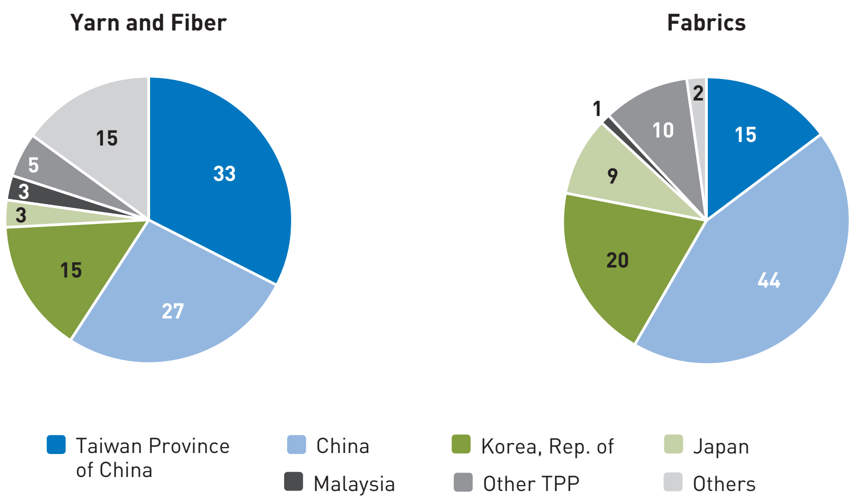
**3) ODM (Original Design Manufacturing)**
This method entails purchasing fabric and materials, cutting, sewing, finishing, packaging and shipping products. The ability to design reflects a higher level of knowledge by the providers and therefore brings higher added value for products. ODM businesses create designs, finish products and sell them to buyers, which are most of the major brand owners in the world.

**4) OBM (Original Brand Manufacturing)**
This method of production is an improvement over OEM, as the manufacturers are responsible for their own designs and sign both domestic and foreign goods supply contracts for their own brands. Under the OBM method, manufacturers in developing economies distribute products mainly in their domestic market and in the markets of neighbouring countries.

Source: AJC.

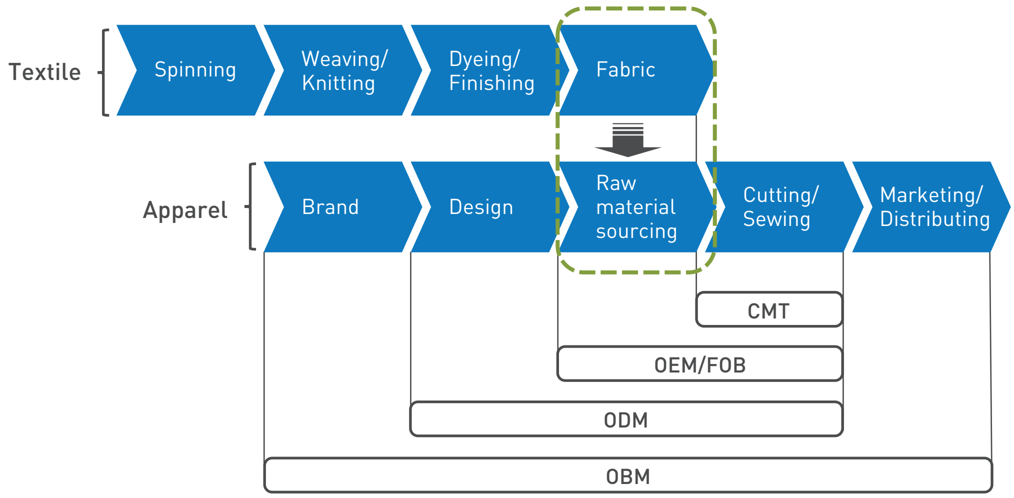
According to a report by the Viet Nam Textile and Apparel Association (VITAS), there are 7,154 textile and garment firms in the country. Of these, approximately 62 per cent (4,458) are garment firms and the other 38 per cent (2,696) are in the upstream or midstream process, 1,204 in spinning and 1,492 in dyeing and weaving. Raw materials are mainly supplied from Taiwan Province of China and China (figure 3).

Figure 3. **Raw materials suppliers for apparel**




Source: AJC based on MRI (2017).
Note: As of 2016. "Other TPP" includes the United States.

Figure 4. **Production mode of textile and apparel industry**




Source: Bui Van Tot (2017).

Vietnamese companies are not involved in stocking material, designing or building garment sales channels, or marketing (figure 4). This means that they have low levels of business risk, but also that the production they perform provides little value added and is not knowledge-intensive. In Viet Nam, the value added of garment manufactures gained through CMT activity seems to be only 5 per cent of total value added. Materials and secondary materials such as fabric and accessories account for 8 to 9 per cent of total value added; the remaining amount is acquired by companies in developed countries that handle planning and distribution. Firms in developing countries are in general contracted for low value added production and distribution formats, and Viet Nam is no exception.

For Viet Nam, the key to its development strategy is to produce more advanced processes, products or functions within global production and distribution networks. It is also important to have knowledge-intensive functions such as design and brand formation or distribution development. However, at present, the lack of large-scale, well-developed systems, which can be seen in labour disputes and complex, unclear trading procedures, are holding back the advancement of the garment manufacturing industry. With the growth in production values of both textiles and clothing over the past 10 years, the sewing and spinning segments have been expanding rapidly. In contrast, the growth of other segments such as fabrics and fabric-related products are not expanding. This implies that the midstream and upstream processes in Viet Nam are still immature.

The government intends to develop the downstream textile process in Viet Nam. In the domestic textile industry, Ho Chi Minh City and Hanoi have been regarded as high-value apparel manufacturing bases. Thus, the government is aiming to develop upstream and downstream processes in northern and central Viet Nam. Following the initiative taken by the government, it is expected that downstream processing will also develop in Viet Nam. At present most local firms are engaged in OEM; it is expected that they produce and export high-value apparel. Original design manufacturing (ODM) and original brand manufacturing (OBM) modes provide such opportunities, which may come with NEMs. Developing NEMs in the textile and apparel industry is a viable means to create higher value added products.

### (2) Subcontracting: Electronics manufacturing

Although many industries are growing rapidly in Viet Nam, electronics is growing the most rapidly. Viet Nam was poised to export more than $70 billion worth of electronics in 2017, thanks to large investments from electronics giants such as Samsung, LG and Intel. Vietnamese electronics manufacturing firms can play a bigger role in the industrial development of the nation and help the growth of the country's exports, thereby creating more jobs. At present, the industry is dominated by foreign firms. In 2015, $10 billion of FDI into the industry came from multinational corporations, such as Samsung and Panasonic. Foreign affiliates hold 80 per cent of the local market share and produce 90 per cent of electronics exports.

Viet Nam exports great amounts of electronics products to the world but imports many electronics parts. In 2016, for example, it exported mobile phones worth $34.3 billion but imported mobiles and parts worth $10.6 billion (table 3). Leading electronics manufacturers still import the majority of parts, for assembly in the country. According to a 2016 JETRO survey, the local procurement rate in the Vietnamese electronics industry by Japanese-affiliated companies in 2015 was 28.5 per cent (table 4). The share of procurement from Vietnamese companies was only 14.3 per cent.[6]

Table 3. **Viet Nam's major trade items, 2016**

| | Export | Amount (US$ billion) | Share (%) | Import | Amount (US$ billion) | Share (%) |
|---|---|---|---|---|---|---|
| 1 | Phone system devices (including smartphones) | 34.3 | 19.4 | Machinery equipment | 28.4 | 16.3 |
| 2 | Garment | 23.8 | 13.5 | Computers, optical readers | 23.1 | 16.0 |
| 3 | Computers, optical readers | 19.0 | 10.7 | Phone system devices | 10.6 | 6.1 |
| 4 | Footwear | 13.0 | 7.4 | Yarn | 10.2 | 6.0 |
| 5 | Machinery equipment | 10.1 | 5.7 | Iron, iron scraps | 7.5 | 4.6 |
| 6 | Fish | 7.1 | 4.0 | Plastic raw materials | 6.0 | 3.6 |
| 7 | Wood/wooden products | 7.0 | 3.9 | Fiber and fabric | 5.0 | 2.9 |
| 8 | Autobike/parts | 6.1 | 3.4 | Petrorium material | 4.9 | 2.8 |
| 9 | Coffee | 3.3 | 1.9 | Metal | 4.8 | 2.8 |
| 10 | Bag, Suitcase, | 3.2 | 1.8 | Plastic raw materials | 4.4 | 2.5 |
| | **Total (incl. others)** | **176.6** | **100** | **Total (incl. others)** | **174.1** | **100** |
| | Doemstic firms | 52.7 | 29.8 | Doemstic firms | 71.8 | 41.3 |
| | Foreign Firms | 123.9 | 70.2 | Foreign Firms | 102.3 | 58.7 |

Source: General Department of Viet Nam Customs.

6 This is considerably lower than in China (66.2 per cent) and in Thailand (54.8 per cent).

Table 4. **Parts and materials suppliers of Japanese-affiliated companies in Viet Nam, 2015** (Per cent)

| | Viet Nam | Local | Japanese affiliated | Other foreign | Japan | ASEAN | China | Others |
|---|---|---|---|---|---|---|---|---|
| **Total** | **32.1** | 41.2 | 45.1 | 13.7 | **35.5** | **11.9** | **12.1** | **8.4** |
| Food processing | 67.2 | 85.3 | 11.7 | 3.0 | 10.6 | 12.8 | 3.7 | 5.7 |
| Textile and apparel | 29.0 | 39.7 | 29.1 | 31.2 | 33.9 | 9.7 | 16.5 | 10.9 |
| Plastic | 22.1 | 32.2 | 48.3 | 19.5 | 32.1 | 22.4 | 11.0 | 12.6 |
| Transportation | 28.3 | 18.6 | 73.5 | 7.9 | 41.5 | 18.3 | 5.6 | 6.3 |
| Electronics | 28.5 | 14.3 | 59.7 | 26.0 | 21.7 | 12.7 | 30.2 | 6.9 |

Source: AJC based on JETRO (2016).
Note: The figures for local, Japanese-affiliated and other foreign show each as a share of all suppliers in Viet Nam.

Some 610 businesses operate in the electronics sector in Viet Nam, 52 per cent of which manufacture electronics components. The number is not high enough to sustain a healthy electronics industry. To maintain a high share of local content in electronics production, the number of component suppliers should be greater than that of assemblers. Most electronics on the domestic market are either imported as complete build-up units (CBUs) or assembled from imported components. Given that foreign companies account for almost all of Viet Nam's electronics exports, there is a negligible role for local companies in the industry.

Viet Nam's lack of electronics component suppliers is preventing the industry from achieving its full potential. In the process of industrial development, supporting industries play an important role. The supporting industry in Viet Nam is immature compared with those in other countries such as Thailand and Malaysia, and many problems need to be solved. The capacity to deliver the products needed by the industry in Viet Nam is very low. There is not enough local capacity to meet the requirements of foreign firms that might consider building a processing plant in Viet Nam. The number of local companies operating in the electronics industry is still small, and the components and parts available locally are limited to only the basic products. The problem of low-quality products is a fundamental problem of Vietnamese supporting industries. Lack of capital and technology also frustrate their attempts to expand production lines and to improve product quality.

This has led to a difficulty in upgrading the quality of human resources and thereby reduced the competitiveness of Vietnamese products. Firms must rely on imports from other countries, as seen with Japanese firms in Viet Nam, whose products typically have a local content of only 28 per cent. For Samsung, the current local content rate is between 30 and 35 per cent. For all firms, however, most of their suppliers are foreign companies operating in Viet Nam. Local vendors are capable only of finishing the packaging, printing instruction manuals and making plastic components, which all add very low value. Given the high localization ambitions of international manufacturers, the industry needs to strengthen its supporting clusters. NEMs can offer significant opportunities for local suppliers to join the market.

### (3) Outsourcing: IT-BPO services

Viet Nam is becoming a hot destination for outsourcing, thanks to its competitive labour costs and other business environment costs. It was ranked as the sixth most attractive location in 2017 by A.T. Kearney, on the basis of three indicators: finance, human resource skills and business environment. It is highly ranked in terms of its financial index. In early 2016, Hanoi and Ho Chi Minh City continued to rank in the top 20 of the 100 most attractive cities for outsourcing services, according to a Tholons report.

During 2011 and 2016, the software and digital content industry in Viet Nam maintained a 10–15 per cent annual growth rate, two to three times higher than overall economic growth. Exports of software and digital content rose from $1.1 billion in 2009 to $4.6 billion in 2016. Over the years IT-BPO outsourcing companies in Viet Nam have broken into the markets of the United States, Japan and several European countries. Viet Nam has recently become Japan's second-largest software outsourcing partner after China, accounting for about 21 per cent of the market, while the U.S. and European markets have generated growth rates of 20–30 per cent per year. IT industries are concentrated in the metropolises of Hanoi and Ho Chi Minh City.[7]

In terms of personnel costs, in comparison with IT industry salaries in other ASEAN countries, the average salary in Viet Nam's IT industry remains the lowest. According to a report by the Asian-Oceanian Computing Industry Organization, the average salary of newly graduated engineers is $280 per month. For engineers with three years of experience, it is about $550 per month. For middle managers, it is $1,000 per month and for senior managers, it is about $2,000 per month, equivalent to one third of the salary in Malaysia, and one fifth of the salaries in Japan and the Republic of Korea.

Most of the information system companies in Hanoi handle orders from the public sector, whereas those in Ho Chi Minh City focus on overseas offshoring development, which is IT outsourcing such as for development of systems and smartphone applications. Viet Nam is seeing a rise in the amount of orders in this field. In offshoring development, Vietnamese information system companies receive from overseas an order for part or all of the development of operational software for an information system. There are two types of operation consignment: outsourcing offshoring, which uses external resources that are not part of the company's own group, and in-house offshoring, which uses the company's own resources, including its overseas sites, overseas subsidiaries, and other companies and partner companies within the same group (figure 5). The former tends to create NEM linkages.

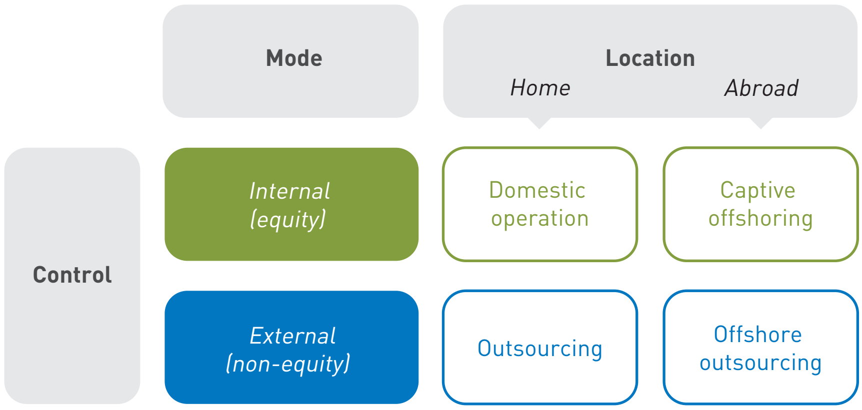
IT outsourcing services generate about $5 billion in foreign exchange a year. However, Viet Nam is still a boutique market when it comes to outsourcing, lagging behind its regional peers such as India and the Philippines, which earned $98 billion and $21 billion, respectively, from providing IT services in 2015. Nevertheless, outsourcing companies in Viet Nam over the years have broken into the markets of the United States, Japan and several European countries.

Japan is the most important client country in IT-BPO. Like China and India, Viet Nam has high growth potential as an offshoring site for information system development. For Japanese companies, the consignment of system development to Viet Nam produces several potential advantages: reduced development costs, resolution of the shortage of domestic system engineers, reduced delivery time and progress toward entering the global market. Information system companies such as Hitachi Solutions and NEC Solution Innovators have thus shifted more business operations into Viet Nam.

[7] Unlike contract manufacturing, service outsourcing contractors are commonly located in cities with developed communications infrastructure.

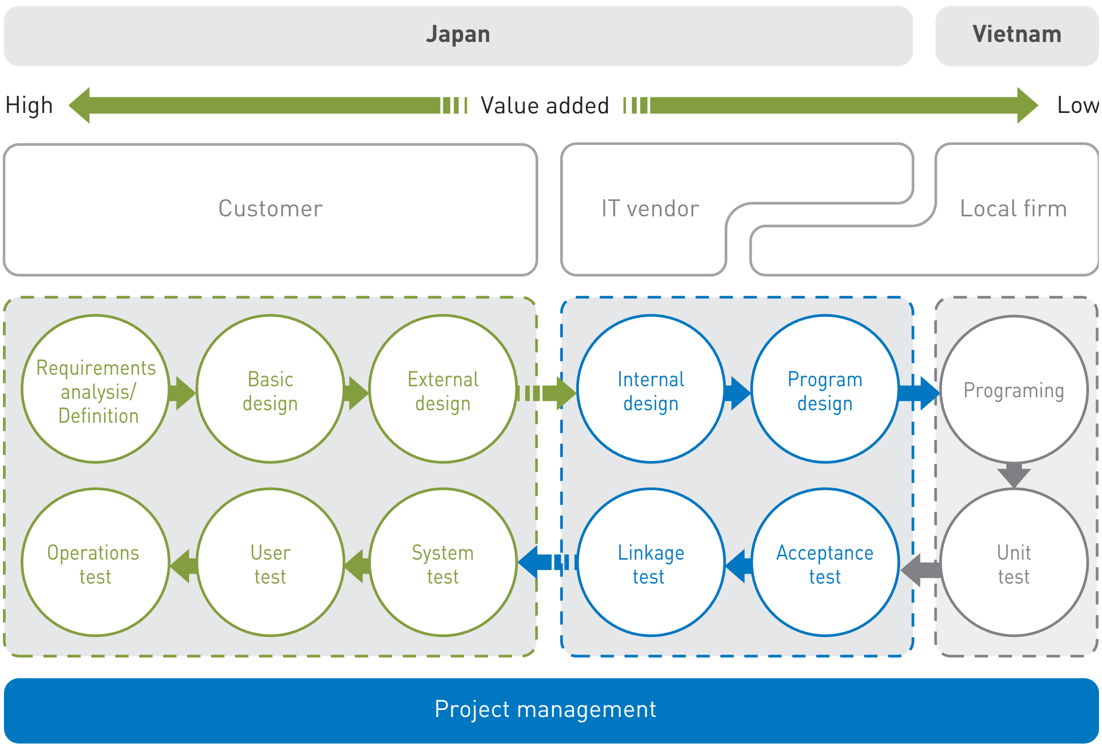
Software development processes use the transaction relationships and development management systems shown in figure 6. At present, many Vietnamese companies fulfil only the stage of low value added work (coding and unit testing).

Figure 5. **Outsourcing and offshoring by type**




Source: AJC.

Figure 6. **Offshoring to Viet Nam IT firms from Japan**

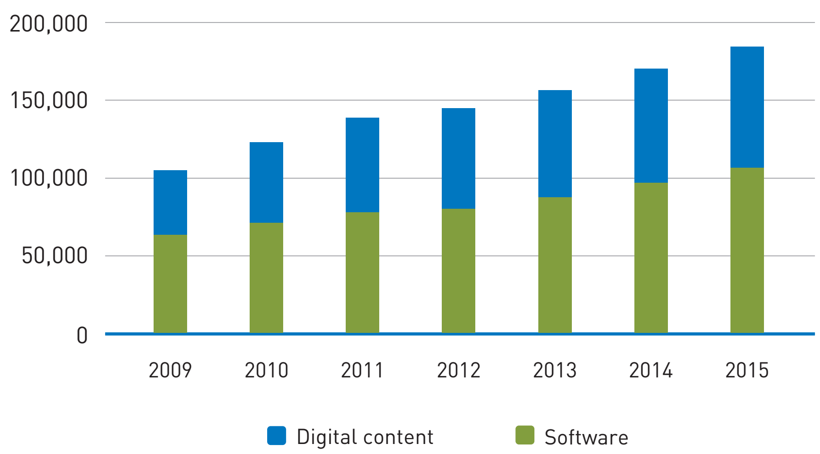



Source: AJC.

Viet Nam's IT-BPO sector is still at an early stage, given the country's relatively late integration of the Internet. But the sector has registered rapid growth and has been moving up the value chain and offering more value added work. Software outsourcing is set to grow faster in the near future, as Viet Nam has become better known as an outsourcing destination.

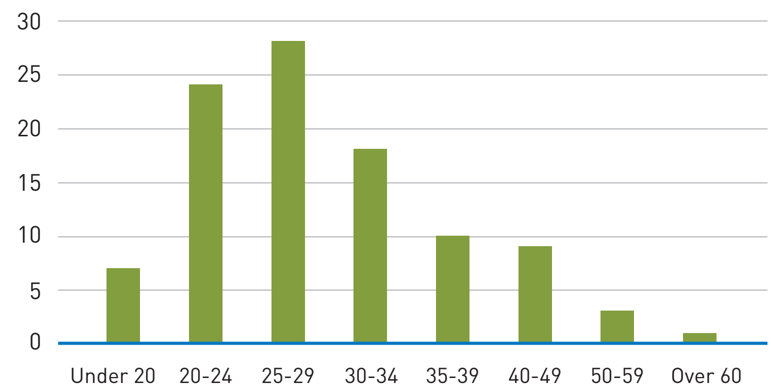
According to the Viet Nam Software Association (VINASA) in 2015, the country required approximately 400,000 more IT workers for the 2016–2020 period. In 2017, it was estimated that about 200,000 IT workers were engaged in the digital and software fields (figure 7). Some 290 universities and junior colleges in Viet Nam as well as 150 other training establishments produce IT workers. Viet Nam is rich in young people with a basic education (figure 8) who have the potential ability to acquire new skills quickly. To maximize the opportunities, a continued focus on workforce training is necessary, as universities currently cannot produce enough high-skilled graduates.

Figure 7. **Viet Nam's digital and software workers, 2009–2015** (Person)




Source: VINASA (2016).

Figure 8. **Age composition of Vietnamese programmers, 2015** (Per cent)




Source: AJC based on VINASA.

As Vietnamese companies generally are small, many with fewer than 500 employees,[8] they can provide services only in specific areas such as application development and testing, customization, maintenance and support, not in end-to-end services or those requiring specialized skills.

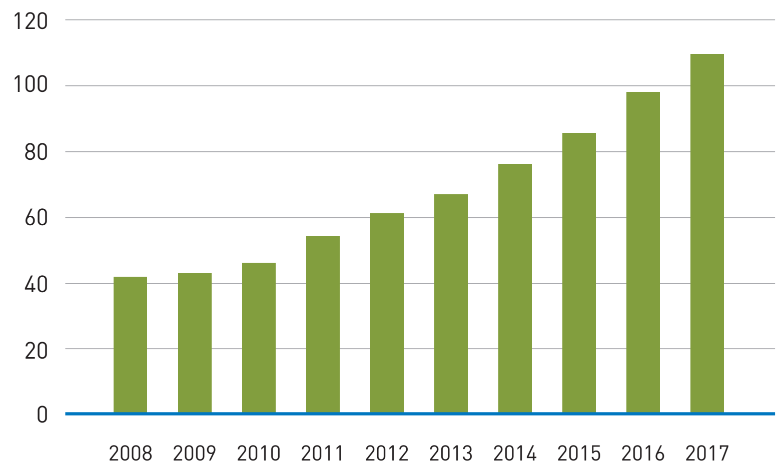
### (4) Franchising: Retail

Since joining the WTO, Viet Nam has emerged as one of the most attractive retail markets in the world. Its stable economic growth and approximately 90 million people provide attractions for the retail sector.

Viet Nam's retail market is one of the region's most dynamic, with high annual growth rates. Its retail industry was forecasted to reach $109 billion in 2017 (figure 9). Many international retail groups have entered the market recently, thanks to the lower trade and investment barriers. Hanoi and Ho Chi Minh City were ranked among the top 10 Asian cities for retail expansion in 2016.

The retail sector in Viet Nam is fragmented and dominated by small, family-owned businesses. It is facing a structural change, from a traditional shop to a contemporary store. According to Euromonitor (2016), traditional retail shops accounted for roughly 95 per cent of all retailers and only 5 per cent of retailers were modern retail shops. However, the number of modern retail outlets has been growing in urban areas. Statistics from the Ministry of Industry and Trade show that more than 700 supermarkets, 125 shopping centres and 8,600 traditional markets are in operation throughout Viet Nam. Of these, 4 per cent of the supermarkets and 25 per cent of the shopping centres are owned by foreign businesses. The research firm IGD estimated the annual growth of the retail sector for 2018 to 2021 at 37 per cent. IGD also pointed out that disposable income in Viet Nam has increased dramatically and that regulations have been amended to encourage foreign investment.

Figure 9. **Viet Nam's retail sales, 2008–2017** (Billion of dollars)




Source: EIU.
Note: Figures for 2017 were forecasted.

[8] As an exception, FPT Software Company was planning to invest up to $200 million in merger and acquisition deals between 2016 and 2020 to boost its workforce to 30,000, according to a company statement.

Consumption habits in Viet Nam are changing significantly. Reasons for the growing number of modern retail shops include rising demand for high-quality, hygienic products as incomes increase, and for the convenience of buying various types of product in a single shop. The Ministry of Industry and Trade has estimated that the number of supermarkets will grow to 1,300 within the next 10 years and that the percentage of modern retail stores will rise, especially in urban areas. These changes as well as income growth are accelerating the emergence of modern retailers, which tend to be linked through NEMs with foreign retailers.

FDI is prevalent in the department store business. NEMs (such as management contracts) are rarely observed in relations with foreign department stores, because local firms have limited management skills and know-how. Department stores first appeared in Viet Nam in 1999, and there are now 13. The first was Diamond Plaza, a Singapore–Korea joint venture in Ho Chi Minh City. This was followed by Parkson, a Malaysian department store; Robinson's, a Thai department store; and Lotte, a Korean department store. In 2016 Takashimaya, a Japanese department store, was also opened.

Foreign-owned supermarkets such as Metro and Big C entered the Vietnamese market from the late 1990s to the early 2000s. Metro, a German supermarket chain, was acquired by the TCC Group, a major Thailand financial conglomerate, in 2014, and in 2016 the French supermarket Big C was purchased by a Thai company, the Central Group. As a result, many Thai products are imported into Viet Nam; the TCC Group plans to increase the share of Thai products at Metro to 60 per cent. Japan's AEON opened a store in Ho Chi Minh City in 2014, and as of August 2016 it operated four locations in Viet Nam.

In Viet Nam, the number of convenience stores is increasing dramatically through the use of franchising. As of February 2017, the total number of stores of the six major convenience store companies had increased to 1,634, nearly four times more than in 2015 (table 5). Along with economic growth, the demand for modern distribution stores has increased, and the number of convenience stores is rapidly expanding (box 3). In particular, Japanese convenience stores are expanding. Franchising is well known as a method of marketing and distributing products or services. In box 4, FamilyMart's franchise agreement in Viet Nam is explained.

Table 5. **Convenience stores in Viet Nam, 2015 and 2017**

| Convenience Stores | Est. | 2015 | 2017 | | | |
|---|---|---|---|---|---|---|
| | | | | Ho Chi Minh City | Hanoi | Other |
| VinMart+ | 2014 | 100 | 950 | 400 | 400 | 150 |
| FamilyMart | 1981 | 73 | 133 | 122 | 0 | 11 |
| MiniStop | 1980 | 17 | 71 | 71 | 0 | 0 |
| Circle K | 1961 | 104 | 211 | 153 | 54 | 4 |
| Shop&Go | 2005 | 127 | 119 | 101 | 18 | 0 |
| B's Mart | 2013 | 98 | 150 | 150 | 0 | 0 |
| **Total** | | **419** | **1,634** | **997** | **472** | **165** |

Source: Asia Plus Inc., *Shopping Behaviors at Convenience Stores in Ho Chi Minh City.*

## Box 3. **Convenience stores in Viet Nam**

Convenience stores are penetrating the lives of Vietnamese people. Along with consumer style changes and household size reductions, Vietnamese people cite convenience as a reason for choosing such stores. Convenience stores in Viet Nam are air-conditioned, a place to sit and take a rest. The quality of goods is high, and the display is clean. Some stores offer free Wi-Fi service, and they are becoming places where young people gather. More than a third of households are now doing daily shopping at convenience stores and mini-marts.

In 2014, the Vin Group, the biggest real estate conglomerate in Viet Nam, acquired a local supermarket and entered the retail business. The Vin Group has accelerated the business of the convenience store VinMart+ and in 2017 had 950 stores, mainly in Hanoi and Ho Chi Minh City. Although the locations are good, many stores are narrow and contain less than 100 square meters of space. They are commonly operated by two staff people. Their one-day sales are about $700. Major items sold are alcohol and beverages, sweets, and processed foods. The items they sell are almost the same as supermarkets. In the summer after 4 pm, there are processed foods for dinner in the main display and they are discounted by 10 to 20 per cent. Consumers have liked this approach, and convenience stores are acquiring customers from traditional stores. The Vin Group plans to increase the number of VinMart+ stores to 10,000 by 2019.

### VinMart+


### FamilyMart


### Circle K

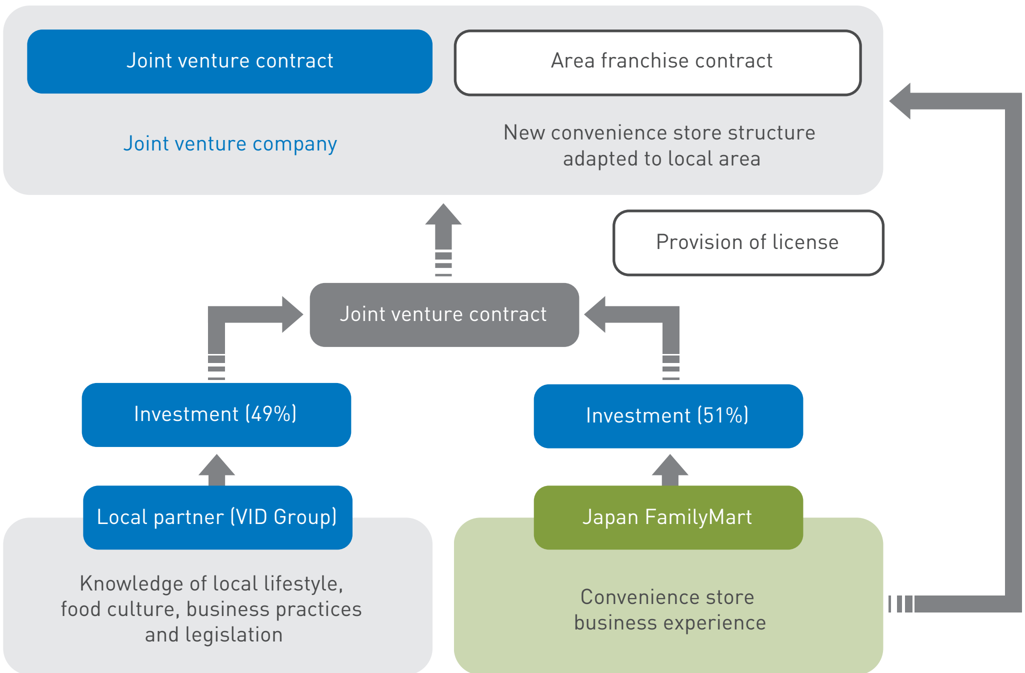

### Shop&Go

## Box 4 . **Franchising agreements of FamilyMart in Viet Nam**

In 2009, FamilyMart entered a joint venture with the Phu Thai Group, a large Vietnamese regional distribution enterprise, but in 2013 the joint venture was dissolved. In 2014, FamilyMart established a new company, FamilyMart Viet Nam Joint Stock Company, in Viet Nam. It intends to expand its stores by the franchise method, using a business model based on Japanese-style convenience stores. As its basic template for overseas expansion, FamilyMart enters into joint ventures with local partners (for example, the VID Group (Viet Nam Investment Development Group)) that have local networks and expert knowledge about local customs and regulations. FamilyMart considers that sharing its know-how with local partners increases the probability of successful business development in the context of Viet Nam's retail industry and logistics infrastructure.

In addition to providing licenses for the franchise, FamilyMart invests in the joint venture (51 per cent ownership) and participates in its management, giving the company a stake in future profits and dividends. FamilyMart also receives commissions commensurate with the value of licenses and the business know-how provided to the local partner. These three sources combine to create a well-balanced arrangement for generating income.

### Box figure 4.1. **Entering into joint ventures with local partners**




Source: FamilyMart, Annual Report 2016.

Government deregulation is also driving the development of multiple stores. Although there is a system for the Vietnamese authorities to examine the impact on local companies of issuing a new retail store permit, the criteria are not made clear. This makes chain development difficult, which also affects NEM development in the retail industry. For example, formerly it was difficult for retailers to increase the number of stores because of the economic needs test established by the regulation, which allows retailers to open a new store only after the number of retail stores and population density in the proposed store area are examined. However, as of May 2016, companies no longer need review by the authorities to open multiple small stores – of 500 m2 or less – in the same area.

In the future, convenience store companies will expand not only to big cities in Viet Nam but also to medium-size cities. The data show that Viet Nam has one convenience store for every 69,000 people, as compared with higher densities in the Republic of Korea (one store per 1,800 people) and in China (one store per 21,000 people).

In addition, there are some barriers related to regulations. In Viet Nam, the regulation on subleasing a commercial facility is not clear. At present, companies can invite tenants to occupy an estate owned with foreign capital, but there is no rule on subleasing to attract more tenants to rented buildings. As the criteria differ depending on the area and even the person in power at the authority, they pose an obstacle to retailers hoping to expand the stores. In addition, the approval process for the establishment of overseas affiliates takes too long, and sales restrictions are applied to items such as alcoholic beverages and tobacco.

Acquiring prime retail real estate remains a challenge in Viet Nam because of disproportionately high rents and a shortage of reliable property managers. There are also problems with poor logistics networks and substandard local suppliers, compounding the supply chain problems and resulting in increases in hidden costs, which may derail the development of Viet Nam as a low-cost market. Franchised operations and joint ventures by foreign retailers help mitigate these issues, whereas the commitment of local firms or local suppliers is essential for NEM operations.

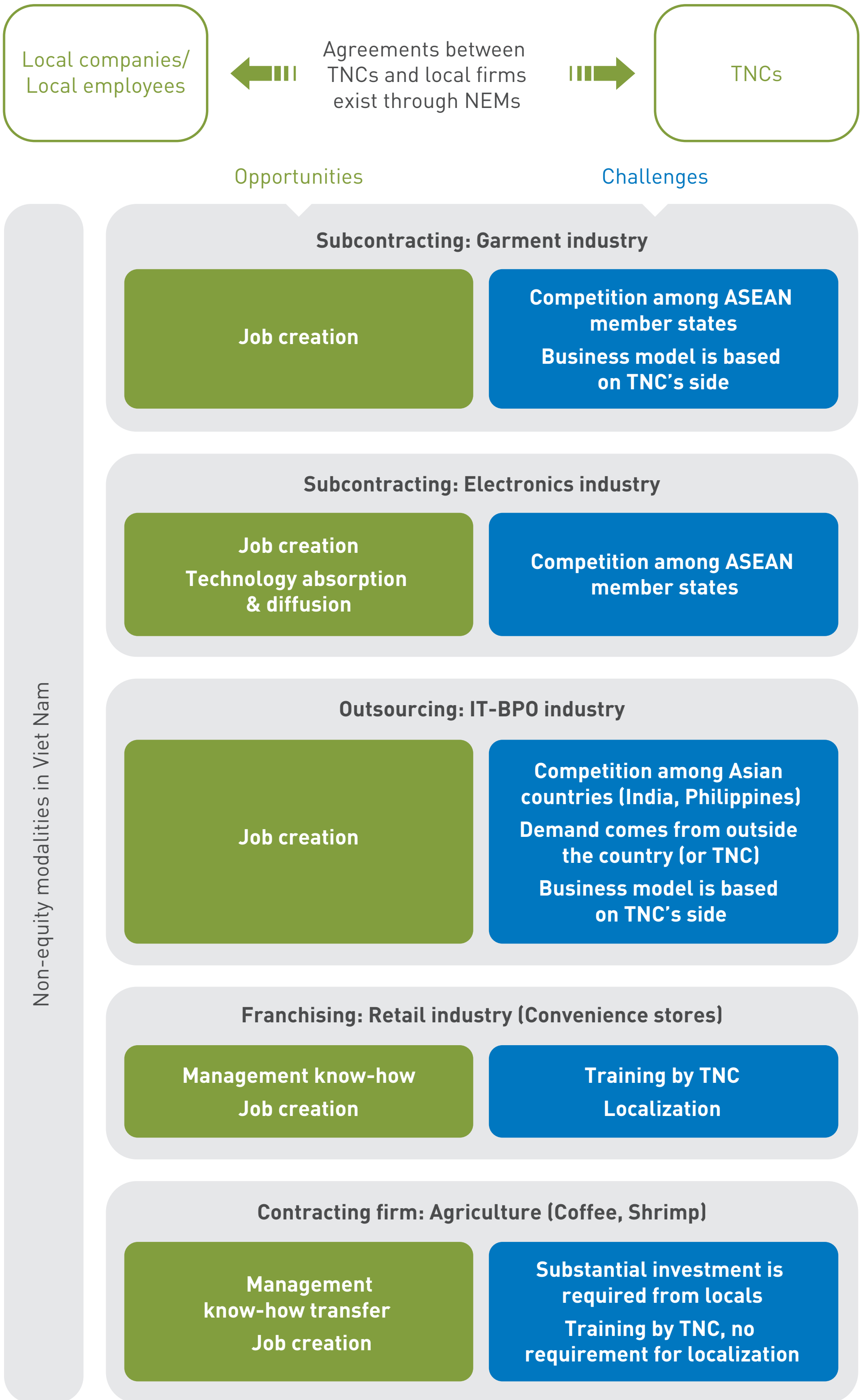
# 3. OPPORTUNITIES AND CHALLENGES FOR NEM IN VIET NAM

This section provides an analysis of opportunities and challenges facing Viet Nam in promoting and utilizing NEMs (figure 10). By establishing NEM agreements with TNCs, each industry will benefit from a number of opportunities. However, NEMs also bring challenges for local firms.

As with FDI, factors that make locations attractive and conducive to NEMs include political and social stability, sufficiently refined competitive policies, incentives for operations, smooth trading procedures and strong macroeconomic policy. In this regard, Viet Nam has steadily developed its economic institutions and can deal with promoting NEM activities, especially with its abundant, low-cost workforce. While TNCs can enjoy the low labour cost, the government can help ensure job creation (see table 2).[9]

[9] In addition, along with NEM activity, employment may be indirectly created through the spread of related industries. For instance, in the retail sector, further employment is created by local service providers for NEM operations, such as logistics companies and advertising firms (in the future).

Figure 10. **Opportunities and challenges for NEM**




Source: AJC.

One of the salient features of NEMs is that TNCs do not directly own the business activities of local firms but have indirect control of the activities. Non-possession by TNCs provides many potential opportunities for local companies. Using NEM operations, Vietnamese firms can gain the opportunity to participate in GVCs. However, NEM contracts are not guaranteed for long periods. A TNC can use a NEM partner as a test case before full-scale entry, but it can also easily withdraw, as the sunk costs are minimal. In such a case, technology, market access, job creation and stable income do not continue over the long term. Local NEM firms thus face not only opportunities but also challenges. The issues are various: business continuity, characteristic NEM issues, capacity-building, initiative and local embeddedness (table 6). If local NEM firms can strategically use TNCs' know-how and technological skills by linking with them, they can build capacities to deal with these challenges.

*NEM characteristics*

TNCs can find their partners both in and outside the country through, for example, vendor databases and matching events, and can use NEM operations more easily than FDI. For local partners, NEMs make it easier to explore a new market under a contract with TNCs even if demand is not created in the Vietnamese market. Viet Nam exports many garments to developed countries as subcontracted products and also exports IT-BPO services such as software development to Japan, the United States and others. NEM partners can be useful in several ways including providing access to resources they have that are not available in the client country. However, it is difficult to manage the volume of products or services as markets and demands may change dramatically. For example, in the electronics industry, if a TNC changes an electrical product to a new model that requires some input not available through the current NEM partner, it may end the contract with that partner.

Table 6. **Opportunities and challenges for local firms engaged in NEM**

| Opportunities | Typical industries concerned | Challenges |
|---|---|---|
| **Business continuity problem** | | |
| Easier to find TNC partners both in and outside the country through, for example, vendor databases and matching events. In the retail industry TNCs require local partners that are strong and judicious, capable of taking on risk on behalf of the TNC. | Subcontract manufacturing, IT-BPO, retail | Easier for TNC to terminate the contract and the long-term relationship is not guaranteed, if local firms in other countries are more competitive (e.g. cheap labour costs in Cambodia or Myanmar). |
| **NEM's characteristic issues** | | |
| Easier to enter a new market or new area even though local demand is not yet created in the country. Resources that are available in the country (e.g. export of subcontracting products such as garments, electronics and IT-BPO services contribute to developing the country economically).<br>Resources that are available in the country but are not required there can be usefully utilized outside the country. | Subcontract manufacturing, IT-BPO | Difficult to manage the volume of products or services as market and demand change drastically (e.g. with a change in product model in electronics). |

.../

Table 6. **Opportunities and challenges for local firms engaged in NEM** (Concluded)

| Opportunities | Typical industries concerned | Challenges |
|---|---|---|
| **Capacity-building issues** | | |
| Many opportunities for local firms to develope new business and boost sales.<br>Easier for local employees to work in NEM activities, even with low skills. They may be able to improve their skills through working. | Subcontract manufacturing, IT-BPO, retail | TNCs' technical and managerial support may be limited because of the non-capital relationship. TNCs offer only low-skilled work to NEM partners, so workers' skills improve very slowly. If TNCs withdraw their facilities, workers lose jobs. |
| Diffusion of technology can promote technological enhancement and, through it, can promote the involvement of local firms in global value chains. | Subcontract manufacturing, IT-BPO | Generation and dissemination of technology is an important activity for capacity-building in technology-related NEMs. However, it is not easy for local firms to build further capacity apart from receiving orders from customers, as they obtain only relevant know-how at most. It is important for them to increase production volume and to improve supply chain connectivity by reducing logistical restrictions. |
| **Initiatives and local embeddedness issues** | | |
| Local firms can expand their businesses by using the brands of TNCs. They do not need to consider brand value and management. | Subcontract manufacturing, IT-BPO | Local firms may lose initiative and design ability and be unable to build further capacity in management or marketing (e.g. in the IT-BPO/BPM industry and hotel industry local firms may follow TNCs' business models as they do not need to implement localization strategies). |
| Local firms need to take the initiative for activities that lead to operations and embed knowledge while maintaining the TNC's basic strategy. Through these activities, they can open up new business opportunities and improve management capability. | Retail | It is not easy for local companies (franchisees) to adopt TNCs' original strategies to localize. Local companies need to learn through operating. |

Source: AJC.

### *Capacity-building*

NEMs offer local firms many opportunities for new business and sales growth. It is also easy for local employees to work by subcontracting even if they are low skilled. The diffusion of technology from TNCs can promote technological enhancement in local firms and, through it, the involvement of local firms in GVCs.

Local firms may be able to improve their skills through NEM activity. However, TNCs' technical and managerial support may be limited, owing to the key characteristic of NEMs, i.e. the non-capital relationship between the TNC and the local firm. As TNCs offer only low-skilled jobs to NEM partners, workers' skills tend to improve very slowly. Moreover, if TNCs withdraw, workers lose jobs.

As described earlier, the generation and dissemination of technology is an important activity for capacity-building in technology-related NEMs. However, it is not easy for local firms to build further capacity apart from through orders received from customers. Local firms need to create opportunities for in-house capacity-building on their own or find outside resources such as government support.

*Initiatives and local embeddedness issues*

Through NEM activity, local firms can expand their businesses by using the brands of TNCs. They do not need to consider the value and management of those brands; therefore, they may lose initiative and design ability and find themselves unable to build further capacity in management and marketing. Local companies may follow TNCs' business models in the IT-BPO industry.

When franchising, local companies may not find it easy to adopt the TNC's original strategy to localize. Local companies need to learn through operating. In the retail sector, TNCs require local partners that are competitive and sometimes more refined in their operations, capable of taking on risk on behalf of the TNC. Local firms thus need to take the initiative for activities that lead to operations and embed knowledge while maintaining the TNC's basic strategy. Through these activities, they can enhance the chance of encountering new business opportunities and improve their managerial know-how.

# 4. POLICY IMPLICATIONS

NEM production can play a major role in international production activities in Viet Nam. In particular, contract manufacturing and processing are popular in Viet Nam mainly because of the country's abundance oft low-wage workers. NEM production also has a major impact on a government's industrial development policy.

According to UNCTAD (2011), in order to maximize the benefits that developing countries can obtain by integrating local firms into a TNC's GVC, policymakers in developing countries need to formulate responses to several important challenges (table 7).

- Integrating NEM policies into the overall picture of the national development strategy.
- Supporting the development of the necessary production capacity for NEMs that can become an actor in the TNC's GVC.
- Attracting more NEMs.
- Overcoming any negative results related to NEMs.

Table 7. **Maximizing development benefits from NEMs**

| Policy area | Key actions |
|---|---|
| Embedding NEM policies in overall development strategies | • Integrating NEM policies into industrial development strategies<br>• Ensuring coherence with trade, investment, and technology policies<br>• Miligating dependency risks and supporting upgrading efforts |
| Facilitating and promoting NEMs | • Setting up an enabling legal framework<br>• Promoting NEMs through investment promotion agencies<br>• Securing home-country support measures<br>• Making international policies conducive to NEMs |
| Building domestic productive capacity | • Enhancing technological capacities<br>• Strengthening human resources<br>• Developing entrepreneurship<br>• Providing access to finance |
| Addressing negative effects | • Protecting labour rights and the environment<br>• Safeguarding competition<br>• Strengthening the barganing power of domestic firms |

Source: UNCTAD (2011), p. 165.

In particular, to encourage NEM activities, two policy areas become important for Viet Nam: facilitating and promoting NEMs, and enhancing the technological capacity of local firms. One requirement is the formulation of appropriate domestic policy for the management of an appropriate working environment. NEMs are based on business contract relationships, so it is important for developing countries to formulate clear and transparent rules that stipulate what should be in these contracts.

## 4.1 Facilitation and promotion of NEMs

Facilitation measures to promote business are important for attracting NEMs as well as FDI. NEMs are facilitated by a clear and stable regulatory framework. UNCTAD (2011, p. 169) noted that, as NEMs are based on contractual relationships, the laws and regulations governing these contracts are an important determinant of NEM, and can constitute either an incentive or an obstacle for this kind of business cooperation. Facilitating and promoting NEMs requires an enabling legal framework and stronger promotion policies.

The cost of labour in the traditional Asian manufacturing hubs (such as China and Thailand) has become relatively high, and Viet Nam is an economical alternative, with an abundant working-age population. Its benefits as a production base or investment destination are widely known. However, it is still an emerging country, with obstacles that can negatively affect business operations.

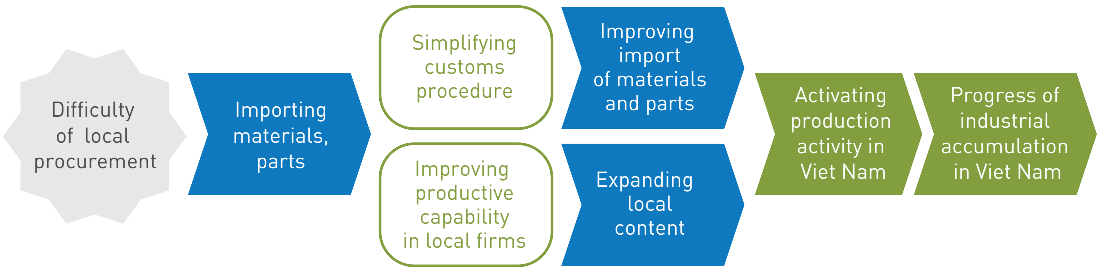
As seen in section 3, many firms operating in Viet Nam now have difficulty procuring raw materials and parts within the country and therefore import them. For this reason, in the garment industry, production is limited to CMT processing, with low value added. In order to increase NEM-related production, local firms must steadily improve their production capacities (see section 4.2). However, it takes time to improve a firm's ability. If firms operating in Viet Nam cannot procure parts and materials locally, the government needs to develop an environment in which parts and materials can be imported smoothly (figure 11). Japanese affiliate firms in Viet Nam point out the complexity of Customs clearance procedures, which are a barrier in the procurement of parts and capital goods from abroad. One example is the import restriction on used machinery.[10]

In order to promote production through NEMs and FDI, it is preferable to relax regulations and facilitate procedures related to imports of raw materials and parts. Although the prohibition on importing used parts and materials is intended to nurture local supporting industries, competition between such imports and local parts and materials makes local production itself more active. This leads to the development of the supporting industry.

Opaque administrative processes and the complex law system pose major difficulties for companies doing business in Viet Nam. The complex commercial law system is hard to comprehend, even for local experts. Thus, the majority of foreign firms need help from professional legal consultants in their operations.

10 This measure is stipulated by the Ministry of Science and Technology Notice (Circular 23/2015/TT - BKHCN). In principle, imports of machinery used for more than 10 years are prohibited. Many Japanese firms import the machinery used in China and other countries into Viet Nam, but some of these machines are properly maintained even if they are more than 10 years old. Although these machines can withstand usual use, Japanese firms cannot import them into Viet Nam.

Figure 11. **Responding to local procurement difficulties**




Source: AJC.

There is no specific legal framework for NEM. However, the government needs to simplify the procedures for launching a new business. Doing so would also help in attracting FDI. In the retail industry, it takes a long time to get some regulations approved owing to concerns from various stakeholders, resulting in more burden on the operator than in neighbouring countries. In this respect, as with FDI approval, establishing a one-stop service approach by which registration procedures are handled in one agency can shorten the time required for establishing new firms and can reduce costs. The investment promotion agency could play an important role in promoting both NEMs and FDI, as they are related and even established at the same time. Providing information on relevant regulations through the agency website could contribute to the facilitation of business.

Infrastructure is another obstacle. Roads are often narrow and jammed with traffic, which causes delays and extra costs for operations. This especially affects the retail sector, as delivery time is a paramount concern. Maintenance of the road network is indispensable from the viewpoint of the activation of logistics, especially in rural areas with bad connections to main highways, airports and seaports. For Viet Nam to be able to attract NEMs and FDI, there is a need to speed up infrastructure development, especially in transport, power and communications, where it lags behind more developed ASEAN member countries. In addition, regional integration agreements would encourage harmonization and institution-building, and support the establishment of regionally integrated production networks and value chains. As a result, they would promote NEM activities.

Viet Nam will face both opportunities for growth and challenges from the ASEAN Economic Community (AEC). Established in 2015, the AEC will create a single market with free flow of goods, services and investment within the region. Once the AEC is fully established, Vietnamese exports to ASEAN countries can expand through the use of low-tariff and non-tariff privileges. This is a big opportunity for Viet Nam. A competitive economic region will help to improve Vietnamese firms and expand their production. However, the AEC may cause severe competition among the member states. Viet Nam has to compete with others in the region with its own human resources, capital resources and management capacity. Moreover, in various industries where NEMs are used to a large extent, such as retail, for convenience stores – as well as in a broad range of other services fields – it is recommended that the restriction on foreign investment could be eased . As a result, Viet Nam would attract foreign investors as a business destination for service industries.

## 4.2 Improving productive capability

Development strategies related to NEMs become meaningful only if firms in developing countries are qualified as NEM partners of TNCs. In this context, it is important for developing countries to have policies for productive capacity-building, including a strong education policy. Issues related to human capital and technological capacity in Viet Nam are discussed in the following subsections.

### 4.2.1 Strengthening human capital

Investment in human capital is closely associated with creating a more attractive destination for foreign firms, in both NEM activity and FDI. The current education and vocational training system in Viet Nam does not produce an adequate level of skills in the workforce. This reduces the country's competitiveness and makes Viet Nam less attractive for medium- and high-technology manufacturers looking for suitable production bases. Local firms need to implement continuous training to address current and future customer needs. As most Vietnamese firms are medium or small in size, the government needs to consider establishing a public training centre. Under the AEC, Viet Nam will have to open its doors to skilled labour from other ASEAN members, and this will put a strain on Viet Nam's labour force. Vietnamese workers cannot compete with others in the region unless their professional qualifications, foreign language skills and soft skills are improved.

In general, NEMs that are focused on reducing production costs, such as subcontract manufacturing or services outsourcing, have been criticized for their weak employment conditions. In Viet Nam, NEM activities have been accepted positively. In order to keep costs down and remain competitive and attractive for TNCs, local companies may impinge on workers' rights – through low wages, excessive overtime, job instability and poor health care. At the moment, these issues seem not to be coming to the forefront. However, the Vietnamese government needs to constantly monitor these issues to protect workers from unreasonable conditions.

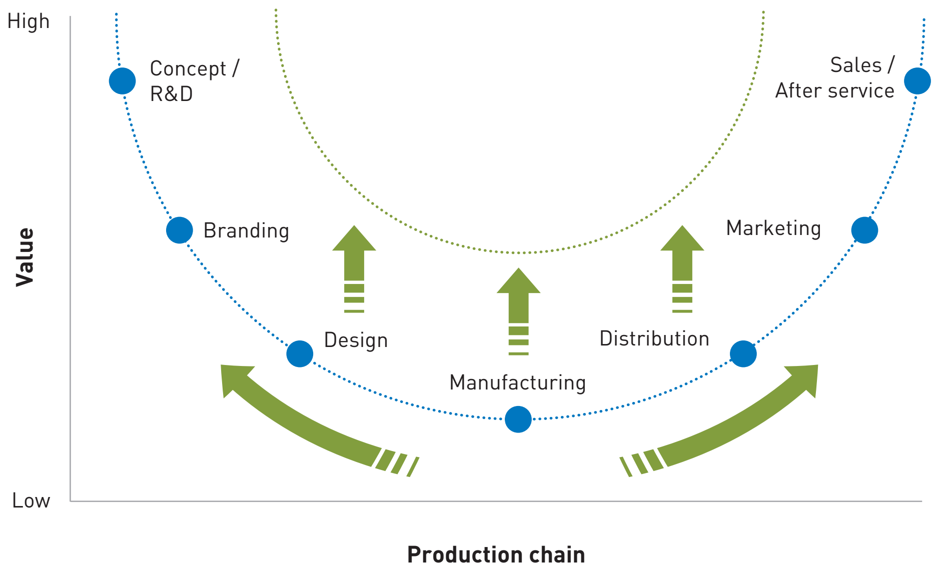
### 4.2.2 Enhancing technological capacities

As noted, the low cost of labour is one of the main reasons why TNCs outsource production to Viet Nam. However, if Vietnamese firms cannot move up the technology ladder and towards higher value added activities, TNCs may terminate NEM contracts. Although basic skills are required in order to move Viet Nam along its path to industrialization, the country should make continuous efforts to improve those skills.

In terms of the value added in each business process, the upstream segments of R&D and parts manufacture and the downstream segments of maintenance and after-sale service are relatively high in value added, but the midstream of the production chain creates low value added (figure 12). At present, most local firms are responsible only for assembly and subcontracting functions. Local firms need to move towards higher value added activities by improving technological capability and capital equipment.

Technological policies are essential to avoid local firms being limited to low value added activities in NEMs. The dissemination of technology is an important activity for capacity-building in technology-related NEM. It can promote technological enhancement and also promote the involvement of local firms in GVCs. The promotion of partnership between local firms and foreign firms may be useful for the dissemination of key technologies, products, processes or management practices. Building a strategy on acquiring abilities and comparative advantages through the effective use of technological policies facilitates connectivity with the broader business world. In the long term, these efforts will enable domestic NEM contractors to become NEM creators.

Figure 12. **Production chain and value added**

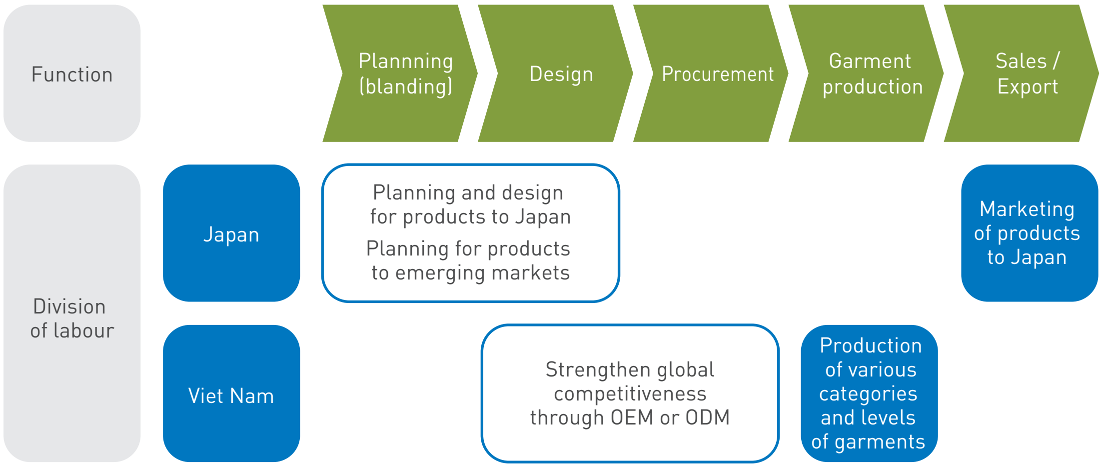



Source: AJC.

In Viet Nam, spillover effects from foreign firms to local firms are considered to be small because of the small amount of linkages with the local economy, as demonstrated by the low local procurement rate. Growing as a production base for foreign firms brings substantial benefits in terms of exports and employment, but developing Viet Nam's domestic industries remains a major challenge. Investments by foreign companies in upstream processes, as well as in large firms, could have spillover effects on the development of domestic industries.

Many garment manufacturers in Viet Nam are still engaged only in CMT processing, and, as noted earlier, about 80 per cent of raw materials are imported from other countries. A representative of Viet Nam Intel Products commented, "The coordination of components in Viet Nam will still take at least 5 to 10 years." However, some local firms are seeking to shift to ODM and OBM. So far, Japanese firms that outsource have been limited to part of the downstream process of production (figure 13). In the apparel industry, local firms want to establish partnerships with Japanese firms to obtain high-quality fabric made in Japan. In addition, they are interested in the design and planning capacities of Japanese firms. Through the growth of Japanese mid- and upstream manufacturers in Viet Nam, local firms can gain opportunities to procure Japanese fabrics in Viet Nam and export finished products, while Japanese companies use the production and sales base in Viet Nam to pursue their business opportunities.

Figure 13. **Functional structure of apparel products and division of labour between Viet Nam and Japan**




Source: AJC based on NRI (2016).

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Within the overall policy framework of NEMs articulated here, the Vietnamese government may want to evaluate the state of NEM or NEM-like operations in the country. Assuming that no such evaluation methodology exists, the AJC proposes the checklist in table 8. The AJC's proposal is based on the corporate code of conduct of the Tokyo Chamber of Commerce and Industry. It provides some tips for the Vietnamese government to use to check whether NEM agreements and operations comply with a certain level of international standards from the viewpoints of NEM foreign clients, NEM local firms, NEM local firms' subcontracting firms and local employers.

Table 8. **Checklist for NEM agreements and operations to maximize benefits from and minimize costs with NEM**

| | | |
|---|---|---|
| NEM policy of Vietnamese government | Compliance with laws | Whether there is an agreement on contract performance |
| | | Whether there is an agreement on contract terms (duration) |
| | | Whether there is an agreement on contract termination and its process |
| | | Whether there is an agreement on contract arrangement (additional contract) and its process |
| | Respect for human rights | Whether there are rules on non-discrimination |
| | | Whether there are rules on basic human rights |
| | | Whether there are rules on harassment (power balance exist between local NEM firms and TNC) |
| | Environmental considerations | Whether there are guidelines on air pollution by local NEM firms |
| | | Whether there are guidelines on water contamination by local NEM firms |
| | | Whether there are guidelines on environmentally friendly goods or services by local NEM firms |
| | Work environment | Whether there are employment rules (laws) on ages under the NEM agreement |
| | | Whether there are employment rules (laws) on gender under the NEM agreement |
| | | Whether there are guidelines on a safe and pleasant work environment for local NEM firms |
| | | Whether there are employment rules (laws) on working environments under the NEM agreement |
| | | Whether there are employment rules (laws) on working conditions under the NEM agreement |
| | | Whether there are employment rules (laws) on working hours under the NEM agreement |
| | | Whether there are employment rules (laws) on taking holidays under the NEM agreement |
| | | Whether there are employment rules (laws) on treatment of absence under the NEM agreement |
| | | Whether there are employment rules (laws) on maternity related leaves under the NEM agreement |
| | | Whether there are guidelines on provision of support system of childcare and nursing care |
| | | Whether there are employment rules (laws) on terminating employment contracts under the NEM agreement |
| | For local firms' development | Whether there is a program which local NEM firms can take to improve their technology or capacity |
| | | Whether there is a program which local NEM firms' employees can learn |
| | | Whether there is a program which local NEM firms can take to understand NEM policy |
| | | Whether there is a program which local NEM firms can take to understand business environment of the industry |
| | Subcontractors and suppliers | Whether there are guidelines for similar NEM policy for local subcontractors and suppliers |

.../

Table 8. **Checklist for NEM agreements and operations to maximize benefits from and minimize costs with NEM** (Concluded)

| | | |
|---|---|---|
| For TNCs, required by the Vietnamese government | Earning the trust of customers and consumers | Whether there are guidelines for TNCs to provide correct information on their products or services |
| | Mutual growth with partner companies | Whether there are guidelines for TNCs to respect free and fair trading rules |
| | | Whether there are guidelines for TNCs to provide relevant information required for trading |
| | | Whether there are guidelines for TNCs to develop relationships based on trust with local NEM firms |
| | Coexistence with local communities | Whether there are guidelines for TNCs to establish and maintain a good relationship with local community where NEM local firms are located |

Source: Adopted from the Tokyo Chamber of Commerce and Industry (2013).

# 5. POSTSCRIPT[11]

An interactive dialogue among Masataka Fujita (Secretary General of ASEAN-Japan Centre), Anh Duong Nguyen (Director of the Department for Macroeconomic Policy and Integration Studies, Central Institute for Economic Management) and Dr. Shunji Karikomi (Assistant Professor, Waseda University) has confirmed (1) the positioning of NEM in Viet Nam and (2) the importance of NEM as well as FDI in the Viet Nam economy. Following the policy recommendation in this country report, we would like to summarize our concluding remarks.

## 5.1 Positioning of NEMs in Viet Nam

NEMs have played a major role in Viet Nam's production activities, in particular, contract manufacturing and processing. As we have seen, textile and garment exports under NEM or subcontract manufacturing are estimated at $20 billion, approximately 11 per cent of total merchandise exports. Electronics manufacturing contributes greatly to expanding the exports of Viet Nam. IT-BPO is also becoming a key export sector. The low cost of labour is one of the main reasons why TNCs outsource production to Viet Nam.

However, as the purchasing power of the middle class has been increasing, in the services sector, NEM activities have been expanding. In the retail sector, international retailers have entered the market, which has more than 92 million consumers, and have been expanding their stores by franchising. Franchising is a well-known method of marketing and distributing special products or services. TNCs and local partners can work together to optimize each other's resources (through international brands and sales networks). The method used for the retail sector can also be applied to hotel and restaurant management, education and a variety of other business types.

[11] The description of postscript was added in reaction to the seminar, "Seminar on Non-Equity Mode (NEM) in Viet Nam – Promoting New Forms of Trade between Japan and ASEAN", held at the Pan Pacific Hotel in Hanoi, Viet Nam on 29 March 2018.

In Viet Nam, the agriculture sector is also very important for NEMs. Viet Nam is one of the leading exporters of seafood and agricultural products, such as shrimp and coffee. A diverse range of agricultural products is sourced through contract farming in Viet Nam. For example, coffee is produced through contract farming with Nestlé. Contract farming helps create a large number of jobs for small-scale farms; it also offers farmers stable sales and incomes.

Viet Nam's comparative advantage is still in cheap labour. The Vietnamese industries that are involved in GVCs are driven by the labour force, rather than technology. If Viet Nam cannot move up the technology ladder and towards higher value added production, TNCs may terminate contracts (in the case of NEMs) or withdraw capital (in the case of FDI). Local firms need to move towards higher value added activities by improving their technological capabilities. This is the challenge for Viet Nam, as in order to have greater employment impact through the use of NEMs.

## 5.2 Importance of FDI as well as NEM

NEM contracts with TNCs offer big opportunities for local partners. However, TNCs are highly volatile and can move easily to another country. As many people pointed out in the seminar, Viet Nam still needs FDI, which can be expected to generate external spillovers in the country. In order to grow the economy, it needs continuous FDI in the manufacturing sector and in other industrial sectors.

Today, many foreign companies invest in Viet Nam, as the country welcomes FDI. Indeed, as a result of foreign companies operating in Viet Nam, the volume of exports has grown significantly. However, Mr. Nguyen pointed out that even if Viet Nam's exports were to rise considerably, the share of domestic value added content in total exports is very low and FDI cannot contribute much to job creation because a large part of FDI is capital-intensive.

Mr. Nguyen stressed that FDI is by no means the only important driver of trade. Viet Nam is revising its FDI policy in the context of economic restructuring. GVCs and NEMs are evolving and gaining more importance in Viet Nam's trade. NEMs can complement FDI in broadening economic opportunities.

What is important in order for Viet Nam to encourage NEM activities? At first, it is important for firms to increase production volume. Greater production volume gives companies better bargaining power. They can make efforts to improve the quality of products while enhancing management skills. It is also important to improve supply chain connectivity by reducing logistical restrictions.

## 5.3 Concluding remarks

NEM activities with TNCs are beneficial for the Vietnamese economy, but they are not enough to ensure economic and social upgrading over time. Local firms need to move towards higher value added activities by improving their technological capabilities. Developing human capital is crucial in order to move into higher value added activities. Local firms need to implement continuous internal training in higher-level job skills; however, most local firms cannot implement continuous or even regular training due to its cost. It would help local firms if there were some support for training.

As mentioned during the dialogue, Viet Nam needs to recognize the importance of NEMs and look for measures to facilitate or promote NEMs in various sectors. Upgraded levels of both technologies and skills are equally important for moving up in GVCs. Capacity-building is critical for all industries. In NEM activities, rather than receiving orders from TNCs, local NEM firms need to build their own capacities and technologies through their own learning systems. This can apply to all modes of NEMs. However, it is not easy for local NEM firms to accomplish on their own. Learning systems supported by the government are necessary in all sectors. With such systems, local firms can build on their own initiative to move up the ladder of GVCs. Through NEM activity, there is no doubt that Vietnamese firms can be further encouraged to participate in GVCs, and Viet Nam needs to promote NEM activity in this respect.

NEM activities contribute to the development of various sectors in Viet Nam. As this paper shows, selected sectors (manufacturing, agriculture, textiles and garments, IT-BPO, retail) have different characteristics and modalities, and there are many ways in which Vietnamese firms in these sectors can get involved in NEMs. These activities may expand further, and local NEM business players must demonstrate the capacity of local suppliers before foreign investors will decide to invest in Viet Nam. NEM activity is very important in broadening economic opportunities, but it also poses risks for companies; the government has to be aware of such risks and watch for ways to minimize them.

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# ANNEX

## Seminar on Non-Equity Mode (NEM) in Viet Nam
## Promoting New Forms of Trade between Japan and ASEAN

Hanoi, Viet Nam, 29 March 2018

| TIME | ACTIVITY |
|---|---|
| 09:00 – 09:30 | **Registration** |
| 09:30 – 09:40 | **OPENING REMARKS**<br>**Viet Nam Trade Promotion Agency**<br>Ministry of industry and Trade |
| 09:40 – 10:10 | **INTRODUCTORY REMARKS ON NON-EQUITY MODE OF INTERNATIONAL TRADE**<br>**Secretary General Masataka Fujita**<br>ASEAN-Japan Centre |
| 10:10 – 10:45 | **Photo session/Coffee Break** |
| 10:45 – 11:45 | **REPORT BY JAPAN EXTERNAL TRADE ORGANIZATION**<br>**Mr. Naoki Takeuchi**<br>JETRO Hanoi Office |
| 11:45 – 12:00 | **Q&A** |
| 12:00 – 13:30 | **Lunch** |
| 13:30 – 13:55 | **REPORT OF INDUSTRIAL SITUATION (TEXTILE AND GARMENT)**<br>**Ms. Hoang Ngoc Anh**<br>Viet Nam Textile and Garment Association (VITAS) |
| 13:55 – 14:20 | **REPORT OF INDUSTRIAL SITUATION (ELECTRONIC)**<br>**Ms. Do Thi Thuy Huong (VEIA)**<br>Viet Nam Electronic Industries Association (VEIA) |
| 14:20 – 14:45 | **REPORT OF INDUSTRIAL SITUATION (SOFTWARE AND IT)**<br>**Mr. Le Quang Luong (VINASA)**<br>Viet Nam Software and IT Services Association (VINASA) |
| 14:45 – 15:25 | **PRESENTATION OF DRAFT COUNTRY REPORT**<br>**Dr. Shuji Karikomi, Waseda University** |
| 15:25 – 15:45 | **Coffee Break** |
| 15:45 – 16:05 | **Mr. Anh Duong Nguyen**<br>Director of the Deptment of Macroeconomic Policy and Integration Studies |

| | | |
|---|---|---|
| 16:05 – 16:35 | **INTERACTIVE DIALOGUE** | |
| | **Facilitator:** | **Secretary General Masataka Fujita**<br>ASEAN-Japan Centre |
| | **Commentors:** | **Dr. Shunji Karikomi** |
| | | **Mr. Anh Duong Nguyen** |
| 16:35 – 16:50 | **SUMMARY AND WRAP UP** | |
| | **Secretary General Masataka Fujita**<br>ASEAN-Japan Centre | |

**END OF THE SEMINAR**
**Mr. Yasushi Ishida**
ASEAN-Japan Centre
Master of Ceremonies

ASEAN-Japan Centre

ASEAN Promotion Centre on Trade, Investment and Tourism
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