Non-Tariff Measures in the European Union-Vietnam Free Trade Agreement: Opportunities and Challenges for Vietnam's Garment and Textile Exports

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Abstract

This paper provides a SWOT analysis of implementation of European-Vietnam Free Trade Agreement (EVFTA)'s non-tariff measures (NTMs)and makes policy suggestions for the Vietnamese government and businesses on the way forward. Research results confirm that Vietnamese garment and textile businesses have gained significant benefits in terms of improved competitive advantage from tariff elimination, more opportunities to expand the EU market share, attracting foreign direct investment on domestic supporting industries, and upgrading modern and environmental-friendly technologies.

However, they are also facing challenges, especially requirements on technical barriers to trade, sanitary and phyto-sanitary measures, and rules of origin. It is recommended that the government should formulate long-term strategies and directions on investment in raw material production, facilitating localization of raw materials, encouraging changes to higher value-added processes in the value chain, promoting trademarks based on advanced technologies, improving quality assurance, protection of labor rights and environment. Meanwhile, Vietnamese businesses should actively enhance competition capacity through strengthening workers' qualification and skills, diversifying products, and improving marketing and promotion activities.

Keywords: European-Vietnam Free Trade Agreement (EVFTA), Non-tariff measure (NTM), Rules of origin (ROO), Sanitary and phyto-sanitary measure (SPS), Technical barrier to trade (TBT).

Introduction

Vietnam has implemented comprehensive economic reforms since the embarkation of Renovation *(Doi Moi)* in 1986 with a focus on market-oriented institutional reforms, macroeconomic stabilization, and pro-active integration. Thanks to these reforms, Vietnam's economic growth is ranked among one of the highest in Southeast Asia region. As its international economic rankings are increasing, Vietnam becomes a reliable destination for foreign investors. This is even more crucial in the context of Covid-19 outbreak when many countries tend to diversify their supply network in the global value chain to minimize risk of disruption caused by the pandemic.

As Vietnam is internationally recognized in effective Covid-19 response, many foreign investors have selected the country as a safe destination for moving factories from China and other countries in the region. As a result, Vietnam achieved significant economic growth rates during 2000-2021 despite the adverse pandemic impacts. According to WTO's statistics, Vietnam's exports-imports have surged 170-fold since the beginning of the renovation in 1986, 37-fold since joining the Association of Southeast Asian Nations (ASEAN) in 1995, and four-fold since becoming an official WTO member in 2007 (WTO, 2020). Since Regional Comprehensive Economic Partnership (RCEP) agreement became effective on 1 January 2022, Vietnam is among the most open countries to trade with 15 signed FTAs. Trade openness, measured by trade as percentage of GDP, increased rapidly from 143.8%in 2007 to 196.1 % in 2018 (UNCTAD, 2019).

Vietnam officially joined the EVFTA on 1 August 2020. After more than one year of enforcement, the agreement has proved to be a driving force for EU-Vietnam trade, contributing to economic development of both sides. According to the Ministry of Industry and Trade, despite Covid-19 pandemic's negative impacts on global trade, EU-Vietnam bilateral trade in goods reached USD 63.6 billion in 2021, an increase of 14.8% compared to 2020. This is a spotlight amid the global pandemic as observed by the European Chamber of Commerce (EUROCHARM) in Vietnam.

As key export products from Vietnam to the EU, according to the Ministry of Industry and Trade (MoIT), garment and textile enjoy great benefits from the agreement with 77,3% of tariff lines reduced within 5 years and the rest removed after 7 years (MoIT, 2020). In addition, EVFTA promotes Vietnamese garment and textile businesses to access to high-quality equipment and materials from EU in compliance with international standards. However, at the same time, Vietnamese garment and textile businesses also face challenges in market access to the EU set out by NTMs, of which most prominent measures, especially technical barriers to trade (TBTs), sanitary and phyto-sanitary measures (SPSs), and rules of origin (ROOs).

As analyzed in the literature review in the following part, most of relevant research works on EVFTA's impacts were conducted before EVFTA became effective. In addition, there are only a few of research works on EVFTA's impacts on garment and textile. Accordingly, the most recent paper on EVFTA's opportunities and challenges for Vietnam's garment and textile exports was released in March 2020. As a result, some policy recommendations are no longer valid in the new context of Vietnam, especially given adverse impacts of COVID-19 pandemic. Thus, the paper fills these gaps with analysis of most updated data and statistics with a focus on the last one year of EVFTA implementation.

Therefore, it is essential to conduct thorough research on EVFTA's NTMs on garment and textile exports to inform policy makers and businesses of benefits and challenges for effective policies and business strategies. This paper aims to analyze the current situation of application of EVFTA's NTMs on Vietnam's garment and textile exports, pointing out opportunities and challenges, and making suggestions for the government and businesses on the way forward.

Based on results of desk study, in-depth interviews and group discussions, the paper then uses collective and synthetic methods to analyze impacts of EVFTA's NTMs on garment and textile exports to make suggestions for the Government and businesses in the sector. Details of expert interviews and group discussions will be analyzed in the subsequent part.

This paper consists of four main sections. In the first section, the authors examine previous research works on EVFTA and its impacts on garment and textile industry, including tariff benefits and NTMs to identify gaps for further analysis and new contributions of this paper. In the second section, the current situation of application of EVFTA's NTMs on Vietnam's garment and textile exports is analyzed and compared with the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) and (the Regional Comprehensive Economic Partnership (RCEP), two other new FTAs joined by Vietnam to understand opportunities and challenges caused by NTMs. The paper then explores details of these opportunities and challenges through expert interviews and group discussions using SWOT approach in the third section. Finally, based on research results, the last section concludes the study and provides policy recommendations to the Government and businesses on how to take advantage of opportunities and mitigate adverse effects of EVFTA's NTMs.

1. Literature review

There are quite a few of national and international papers on impacts of EVFTA on bilateral trade in goods in general, and on garment and textile industry in Vietnam in particular. At the national level, before the agreement officially coming into force in 2020, some scholars analyzed its potential effects, using both quantitative and qualitative measures. Under the EU-Vietnam Multilateral Trade Assistance Phase III (MULTRAP III), a report on "The Free Trade Agreement between Vietnam and the European Union: Quantitative and Qualitative Impact Analysis" not only assessed impacts of EVFTA on investment environment and economic growth in general but also on specific sectors (Philip, *et.al.,* 2011). Subsequently, under the same project, another report was published to provide comprehensive and long-term impacts of EVFTA on the whole Vietnam economy. Using the general equilibrium and partial equilibrium analysis models, the report pointed out EVFTA's trade benefits to Vietnam and challenges that the country might face (Paul Baker, *et.al.*, 2014). Later, in 2017, Paul Baker and his partners continued to examine the potential impact of the agreement, using the Computable General Equilibrium (CGE) model. Simulation results still confirm their previous estimates that Vietnam is expected to gain significantly from bilateral trade liberalization with the EU. Vietnam is benefited from several opportunities for improved integration into GVCs including the cumulation allowance in origin assessment, the reduction in trade facilitation frictions and border administration costs, improved NTMs and enhanced recognition of mutual standards, reduction of tariff lines and improved conditions for investment (Paul Baker, *et.al.,* 2017).

EVFTA's impacts on Vietnam's garment and textile is also a popular topic of master and doctoral theses. In her paper on "Impacts of EVFTA on Vietnam's garment and textile trade", Le Thi Thu Trang (2015) also used quantitative and qualitative methods to analyze potential impacts of EVFTA to Vietnam's garment and textile trade. The gravity model quantified the impacts on import and export of Vietnam's garment and textile. However, bilateral trade and trade policies prior to and after EVFTA accession were not analyzed in detail. The doctoral dissertation of Vu Thanh Huong (2017) on "EVFTA: Impacts on bilateral trade in goods and implications for Vietnam" looked at the agreement's impacts on bilateral trade in general and in two selected sectors, including the garment and textile sector, and the pharmaceutical sector.

In a report commissioned for the EU-funded MULTRAP project on "Effective implementation of EVFTA in garment and textile sector", Nguyen Anh Duong analyzed opportunities and challenges for Vietnam's exports to the EU stemming from both tariff commitments to non-tariff measures in EVFTA. Several recommendations on regulatory reform to improve business environment as well as to create incentives for production of input materials are made to the government. Technical transformation and innovation are key to improve quality of garment and textile products so that entering high-quality standard markets like EU would be easier (Nguyen Anh Duong, 2017).

At international level, potential impacts of EVFTA, especially on bilateral trade are assessed by the European Commission and a few of its members. The European Commission conducted a comprehensive assessment of the expected economic impact of the trade agreement between the EU and Vietnam, building on a quantification of economy-wide effects grounded on the use of a CGE model. The assessment was complemented with qualitative analyses of the parts of the agreement that do not directly turn into specific and immediate changes in bilateral trade costs. The CGE model-based simulation confirms that the importance of the economic gains from the agreement is likely to be different for the two parties. EVFTA can create a EUR-six-billion-euro increase in economic welfare in Vietnam by 2035 (relative to a situation without the agreement in place). In the case of the EU, the welfare gain would reach EUR1.9 billion, mostly reflecting improvements in the terms of trade. For both Vietnam and the EU, these are net welfare gains already considering the tariff revenue losses. By 2035, the boost given to bilateral trade flows compared to the situation without the FTA is considerable for the two parties. EU exports to Vietnam are projected to increase by around 29% while Vietnam exports to the EU: grow by around 18%. When it comes to total trade flows, the percentage changes are considerably more important for Vietnam given the greater contribution of the bilateral trade to its total trade. In absolute terms, Vietnamese exports of goods and services to the EU increase by EUR15 billion while EU exports to Vietnam are anticipated to augment by EUR8.3 billion. Notably, it is estimated that EVFTA will increase Vietnam exports to the EU of "wearing apparel" (up EUR5 billion) and “textile” (up EUR929 million) (European Commission, 2018).

The UK Department for International Trade commissioned an impact assessment of EVFTA’s on the UK in 2019. Also using the CGE model, the report estimates that UK businesses will benefit from reduced tariffs and NTMs on both exports to and imports from Vietnam. As a result, UK goods and services price will be more competitive in Vietnam. UK producers will be able to import a greater choice of intermediate goods and services at a lower cost (Baker and Vanzetti, 2019). As these estimates are based on the authors’ interpretation of the EVFTA text and their judgment on the additional market access offered under the agreement, they are subject to a degree of uncertainty.

In May 2020, the World Bank published a report on “Vietnam: Deepening International Integration and Implementing the EVFTA” exploring the issues globalization and the integration of Vietnam into the global economy, particularly through implementation of the EVFTA. The report shows that Vietnam has a much higher number of legal documents, procedures, and forms related to NTMs than comparator countries. This results in higher trade costs on business. Using ad valorem equivalents, which quantify the effect of NTMs in much the same way as the effect of a tariff measure, it is calculated that Vietnam’s ad valorem equivalent of SPS measures is 16.6%, almost twice as much as ASEAN average (World Bank, 2020).

In their article published on the Textile and Apparel Journal in March 2020, Vuong Duc Anh and Hoang Han analyzed potential impacts of the EVFTA on Vietnam garment and textile, making recommendations for businesses in the sector (Vuong Duc Anh and Hoang Han, 2020). However, as the research was conducted before the accession, some recommendations need updating to reflect recent developments in Vietnam-EU trade, including impacts of COVID-19 pandemic.

In brief, it is observed that the above-mentioned studies mostly focus on assessing impacts of EVFTA on bilateral trade or on tariff benefits of the agreement on Vietnam garment and textile export. While potential impacts of EVFTA’s NTMs are referred to in a number of papers, such impacts are neither analyzed in detail nor quantified in a comprehensive manner. At the same time, there is no detailed analysis of EVFTA’s NTMs on Vietnam’s exports in general nor on Vietnam’s garment and textile exports in particular. Noticeably, some recommendations in these studies are no longer valid due to rapid changes of global economy and recent fluctuation of international garment and textile market caused by Covid-19 pandemic. Therefore, this paper will inherit relevant results of research papers on impacts of EVFTA’s NTMs, providing thorough analysis of effects of these NTMs on Vietnam’s garment and textile exports, and making policy recommendations for the Government and Vietnamese businesses in garment and textile industry.

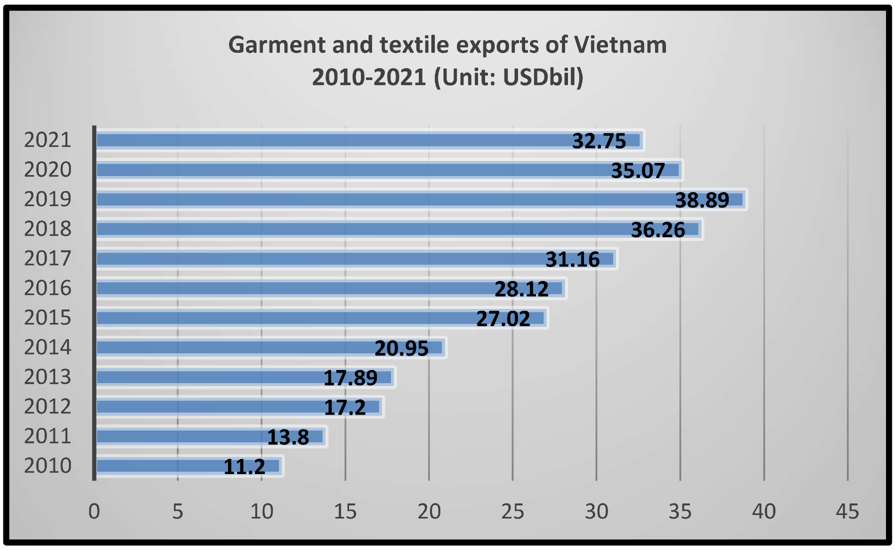
Also, for the first time, main NTMs of three new FTAs of Vietnam, *i.e.,* EVFTA, CPTPP, and RCEP, will be analyzed to form backdrop for policy recommendations on long-term development strategies on how to take advantage of opportunities and to minimize challenges from these NTMs to ensure sustainable development of the garment and textile industry in the context of post-pandemic economic recovery.

2. Current situation of application of EVFTA's NTMs on Vietnam's garment and textile exports

2.1. Current situation of Vietnam's garment and textile exports to the EU

Garment and textile industry has been a very important industry with high export value, accounting for around 12%-16% of annual export turnover of Vietnam in the last decade. Value of Vietnam's garment and textile exports has tripled in ten years from USD 11.2 billion to USD 35.07 from 2010-2020. In 2021, despite adverse effects of Covid-19, the export value still reached USD 32.75 billion.

Figure 1: Garment and textile exports of Vietnam 2010-2021, USD billion



Source: VITAS, GDVC (2021).

Vietnam have remained in the list of top 5 exporters of garment and textile in the world for many years. Main export markets include the US, EU, Japan, and South Korea.

Among the top 5 importers of Vietnam garment and textile products, EU has the largest demand. It is the largest importer of garment and textile products in the world with annual import value of around USD 250 billion, accounting for 34% of total import value of the world. Demand for garment and textile products in the EU market increases around 3% per year. On the other hand, EU also ranks the 2nd in the world, only after China, in exporting garment and textile products, accounting for 24% of the world's total export value. EU member countries often import garment and textile products from developing countries and then re-exports to other countries within EU. Therefore, more than 40% of EU's garment and textile imports are from EU members while the remaining 60% are from non-EU countries, mainly from developing countries. China, Turkey, and Bangladesh have the largest market shares, accounting for 36% of total EU's garment and textile imports with total value of USD100 billion.

Table 1 below illustrates exports of Vietnamese's garment and textile materials of HS57 – HS63 to the EU from 2015 to 2020. It is observed that Vietnam's exports of HS57 to 63 to the EU has been around 11% of total exports to the EU. Under the impacts of Covid-19, exports of HS57 to 62 saw a slight decrease from 2019 as EU consumers tended to reduce consumption of non-essential goods like garment and textile to save incomes for unpredictable future. Meanwhile, exports of HS63 still increased 147%. This might be a result of EVFTA's preferential tariff treatments. Also, Vietnam's exports of HS57 to 63 mainly go to Germany (22%), UK (14%), Netherlands (15%), France (18%) in 2020. This proportion was shifted after UK officially left EU on 1 January 2021.

Table 1: Exports of Vietnamese's garment and textile materials to the EU from 2015 to 2020 by HS code (Unit: USD)

HS/ Year	57 Carpets and other textile floor coverings	58 Fabrics; special woven fabrics, tufted textile fabrics, lace, tapestries, trimmings, embroidery	59 Textile fabrics; impregnated, coated, covered or laminated; textile articles of a kind suitable for industrial use	60 Fabrics; knitted or crocheted
2015	1,156,993	4,088,803	42,585,958	13,586,203
2016	39,624	4,603,408	46,416,972	12,612,334
2017	125,893	5,067,953	47,567,373	13,279,857
2018	7,604,461	4,860,875	44,711,397	15,116,209
2019	31,029,769	4,786,650	54,825,979	17,059,875
2020	47,162,665	5,622,172	42,911,649	8,894,264

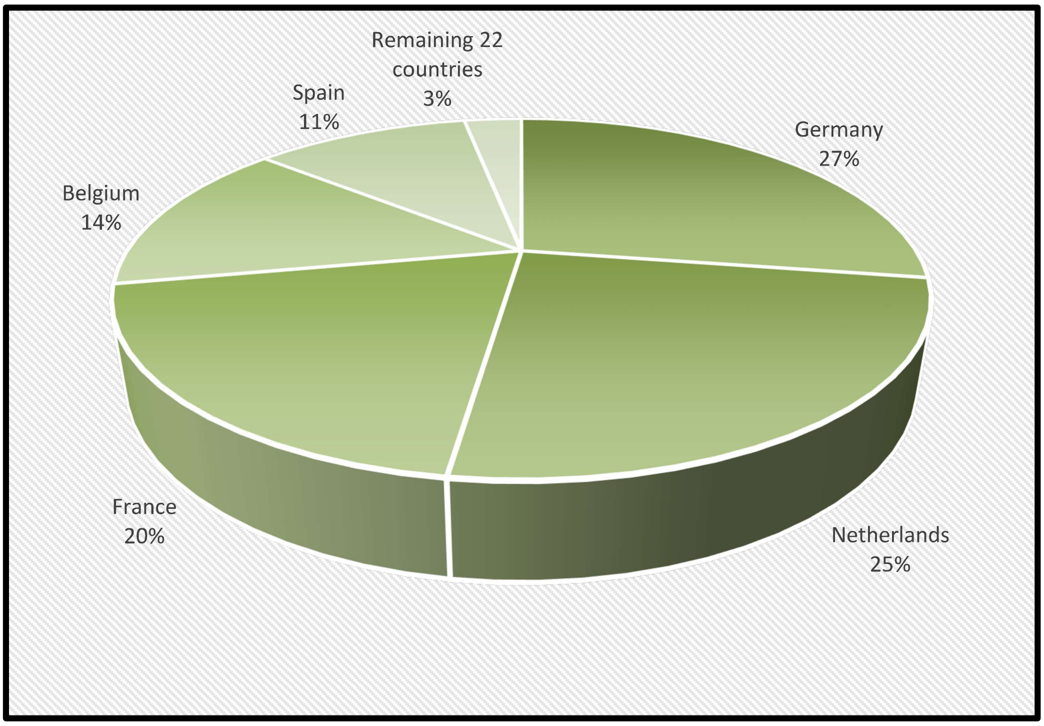
HS/ Year	61 Apparel and clothing accessories; knitted or crocheted	62 Apparel and clothing accessories; not knitted or crocheted	63 Textiles, made up articles; sets; worn clothing and worn textile articles; rags	**Total**
2015	931,527,167	2,478,629,685	215,085,239	3,686,660,048
2016	1,042,198,817	2,472,158,225	212,083,718	3,790,113,098
2017	1,137,376,676	2,596,686,869	216,586,839	4,016,691,460
2018	1,311,592,176	2,788,638,688	236,672,774	4,409,196,580
2019	1,527,329,766	2,741,932,836	261,790,925	4,638,755,800
2020	1,387,308,142	2,226,276,749	646,347,164	4,364,522,805

Source: UN Comtrade (2021).

Despite the increase in total value over the last ten years as mentioned above, Vietnam's garment and textile exports have only accounted for 2-3% of the EU market share. Except China, other countries with similar comparative advantage with Vietnam like Bangladesh, Cambodia or Pakistan are enjoying more preferential tariff treatments to the EU market. Accordingly, Bangladesh and Cambodia are exempted from import tariffs under the Everything but Arm (EBM) programme while Pakistan is also exempted from import tariffs under the Generalized System Preferences (GSP) programme. Meanwhile, Vietnam has only enjoyed a standard preferential tariff treatment of 9.6% under the GSP since 1 January 2014 (Vuong Duc Anh, 2020).

After EVFTA came into force in July 2020, 42.5% of tariff lines for Vietnam's garment and textile exports were removed immediately. As a result, exports to the EU increased in 2021 despite adverse effects of COVID-19 pandemic. According to the Vietnam's General Statistics Office (GSO), Vietnam's garment and textile exports in 2021 are among top eight types of products with export value of USD 32.742 billion, an increase of 9.8% compared to the previous year, ranking 4th after smart phones and accessories, electronics/computers and accessories, machineries, and other spare parts. In 2021, within the EU 27, Germany, the Netherlands, and France continue to be largest markets of Vietnam's garment and textile exports as shown in Figure 2 below.

Figure 2: Vietnam's garment and textile exports to the EU 27 member countries in 2021 (Unit: USD thousand)



Source: VITAS, GDVC (2021).

2.2. Application of EVFTA's NTMs on Vietnam's garment and textile exports

Vietnam's garment and textile exports must comply with commitments on ROOs and other technical and non-technical NTMs in EVFTA. Among these, ROOs provisions are the most challenging requirements. EVFTA's ROOs requirements applicable on Vietnamese exports including garment and textile are based on the GSP scheme but with new and more complicated provisions on determination of origin, acquisition of originating status, origin self-declaration, and origin verification. Therefore, in addition to benefits from general provisions on ROOs, Vietnamese garment and textile export are also subject to stricter ROOs requirements. Noticeably, specific EVFTA's ROOS provisions affecting Vietnamese garment and textile export include cumulation of origin, transit and splitting in a third country, percentage of materials that do not qualify as originating, and product-specific rules (PSR).

Under Article 3 of Protocol 1 of EVFTA, cumulation of origin is applied to fabrics originating in the South Korea provided that Vietnam and this country send a written notification to the EU on application of cumulation of origin and ensure administrative cooperation in verifying the originating status of the products. It means Vietnamese garment and textile businesses is allowed to use raw materials from South Korea as this country has signed FTA with both EU and Vietnam. The Ministry of Trade and Industry (MoIT) issued Circular 11/2020/TT-BCT guiding implementation of ROOs commitments in EVFTA. On 23 December 2020, Vietnam and South-Korea notified to the European Union the undertaking referred to in Article 3(10)(b). Therefore, the two conditions of Article 3(10) are fulfilled and the cumulation in Vietnam for fabrics originating in South Korea provided for in Article 3(7) EVFTA Origin Protocol is applicable as from 23 December 2020. As established by Article 3(9) EVFTA Origin Protocol, the origin of the fabrics originating in South Korea will be declared for the Vietnamese producers by means of origin declarations made out by approved exporters, in accordance with the EU-Korea FTA (European Commission, 2021).

EVFTA also allows splitting consignments at a third country without changing origin provided valid proof of origin is submitted. In this case, customs of importing country might request importers to submit proof of origin under customs supervision of a third country without changing origin such as bill of lading, commercial invoice, sales contract, certification of customs in a third country on non-alternation of origin. This is a new provision of EVFTA that facilitates Vietnamese garment and textile exports to different countries within EU by splitting consignments at a third country if proof of origin is submitted as requested by the importing countries.

As for materials that do not qualify as originating, EVFTA allows flexible use of a small percentage as "tolerance" or *de minimis* of such materials. Specifically, garment and textile products made from 8-10% of *de minimis* fabrics or even up to 20-30% in the case of high-tech fabrics are still qualified as made in Vietnam.

Unlike other FTAs, EVFTA provides for specific operations of insufficient working or processing to confer the status of originating products. Accordingly, whether these operations are combined or performed separately, they are not qualified for originating status. Article 6 of Protocol 1 lists all these operations. Specifically, ironing or pressing of textiles and textile articles is considered insufficient working or processing and thus not qualify for origin preferential treatment.

Relating to product-specific rules (PSR), EVFTA includes 02 annexes on PSR on (i) guiding PSR for all products in general and application on agricultural products, textiles, and oil and gasoline; and (ii) PSR of all 97 chapters. For textiles, “fabric-forward” rule in EVFTA means product materials must be wholly obtained from Vietnam or the EU while the cutting and sewing processes must also be performed at signatory countries. This is a big challenge to Vietnamese garment and textile companies as they largely depend on raw materials imported from non-EU countries. Therefore, the rule on cumulation of origin of raw materials from South Korea might be a flexible solution to the problem of origin for Vietnamese garment and textile export to the EU.

It should also be noticed that in the first two years after EVFTA became effective, Vietnamese exports to the EU still enjoy preferential treatments under the GSP Scheme. Therefore, Vietnamese garment and textile businesses should be aware of these preferential treatments and choose to apply either EVFTA or GSP’s preferential treatments depending on which tariff rates are lower and which ROOs commitments are more suitable to their production from now until 1 August 2022. At the same time, they should be well prepared for transferring to new ROOs commitments after that.

Besides ROOs requirements, Vietnam’s garment and textile products must also comply with other NTMs requirements including technical standards, product safety, labelling of user instruction and country of origin, chemicals used, name of textile fibre and labelling, packaging, and waste from packaging, designing, protective equipment*, etc*. As garment and textile industry uses a variety of chemicals, there are strict requirements and standards on content of these chemicals on fabric, fibre, clothes, and accessories.

In terms of quality standards, Vietnamese businesses are required to comply with ISO 14001. At the same time, EU has strict requirements on material processing and treatment of toxic wastes discharged from planting of raw materials, manufacturing fabrics, processing fabrics, weaving, dyeing, and printing. Packaging of exports must ensure protection of goods during transport from damage caused by mechanical collision, temperature, climate, *etc.* Labelling should provide detailed information on the content of fibres and yarns in the products.

2.3. Application of CPTPP and RCEP’s NTMs on Vietnam’s garment and textile exports

a) Application of CPTPP’s NTMs on Vietnam’s garment and textile exports

The Comprehensive and Progressive Agreement for Trans-Pacific Partnership is an FTA between Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, Peru, New Zealand, Singapore and Vietnam. The CPTPP entered into force on 14 January 2019 for Vietnam. After being in force for all signatories, CPTPP has eliminated more than 98 per cent of tariffs among the eleven countries.

CPTPP has a separate chapter on textile and apparel goods. Like EVFTA, commitments on ROOs are considered the most challenging NTMs. In addition to general provisions on ROOs, specific rules are applied on textile and apparel products. These specific rules provide for use of fibres and yarns wholly obtained in CPTPP areas with an aim to establish supply and investment chains in the region to increase value of textile and apparel goods. In addition, the provision on treatment of short supply list materials flexibly allows use of certain types of fibres and yarns not available in the region.

Under the CPTPP, an importer may make a claim for preferential tariff treatment based on a Certification of Origin completed by an importer, an exporter, or a producer. Unlike other FTAs, under CPTPP, it is not required to follow a prescribed format to apply for certificate of origin. However, it must be in writing (including electronic) and must contain a set of minimum data requirements. CPTPP's preferential ROOs are agreed criteria used to ensure that only goods that meet the CPTPP origin criteria receive CPTPP preferential rates of customs duty set out in the importing Party's Tariff Elimination Schedule. This prevents non-member countries from gaining preferential benefits from the CPTPP. Imports into a CPTPP member that do not comply with the ROOs commitment in the Agreement may be subject to the applied MFN rate of duty instead of the preferential rates available under CPTPP.

A good may be considered to be CPTPP originating if it is wholly obtained or produced entirely in the territory of one or more of the Parties as established in Article 3.3 (Wholly obtained or produced goods); or produced entirely in the territory of one or more of the Parties, exclusively from originating materials; or produced entirely in the territory of one or more of the Parties using non-originating materials provided the good satisfies all applicable requirements of Annex 3-D (Product-Specific Rules of Origin); and the goods must also meet the transit and transshipment rules.

Wholly obtained or produced goods are goods, which are exclusively derived in one or more of the Parties. Typically, these are agricultural goods and natural resources. CPTPP also provides for goods that are made exclusively from wholly obtained or produced goods as being wholly obtained or produced. Goods produced entirely in the territory of one or more of the Parties, from materials classified as 'wholly obtained or produced' or 'originating' under the Product Specific Rules of Origin will qualify for preferential tariff treatment.

Goods that include some non-CPTPP originating materials may still qualify as CPTPP originating, as long as the non-originating materials have undergone a substantial transformation in the territory of one or more CPTPP Parties. These enable a CPTPP Party's customs authority to determine whether a good has undergone sufficient transformation for it to become an 'originating' good.

Compared to other FTAs signed by Vietnam, CPTPP have new ROOs commitments relating to the originating status of sets of goods and remanufactured goods. There are product-specific rules (PSR) for textiles. Accordingly, textile and apparel products of HS Subheading 9404.90, HS Heading 4202, 6601, 7019, and 9619 and HS Chapters 50-63 are subject to additional ROO in addition to the ROO applicable to all other products. Under *De Minimis* rule in CPTPP, a textile or apparel good classified in Chapters 61 through 63 of the Harmonized System that contains non-originating fibres or yarns in the component of the good that determines the tariff classification of the good that do not satisfy the applicable change in tariff classification, shall nonetheless be considered to be an originating good if the total weight of all those fibres or yarns is not more than 10 per cent of the total weight of that component and the good meets all the other applicable requirements. These ROOs requirements have put Vietnamese garment and textile businesses under pressure as nearly 50% of raw materials are imported from China which is not a signatory of CPTPP.

b) Application RCEP's NTMs on Vietnam's garment and textile exports

Signed on 15 November 2020, the Regional Comprehensive Economic Partnership spans all ten ASEAN member countries and China, South Korea, Japan, Australia, and New Zealand. The Agreement just entered into force on 1 January 2022 for ASEAN member countries, Australia, China, Japan, and New Zealand, paving the way for the creation of the world's largest free trade area. As estimated by ADB, 15 member countries of RCEP account for about 29% (USD 25.8 trillion) of global gross domestic product, 30% (3.3 billion) of the world's population, and 25% (USD 12.7 trillion) of global trade in goods and services. RCEP is the world's biggest FTA measured in GDP. The aim is that tariffs will be eliminated on 92% of goods in the next 20 years, and about 65% of the service sector will be open to foreign investors, thereby raising current ceilings on foreign ownership in a range of service sectors. Key features of the RCEP include trade in goods, trade in services, ROOs, trade facilitation, investment, intellectual property, SPS, e-commerce, standards and competition (ADB, 2020).

According to ASEAN Secretariat, the entry into force of the RCEP is a manifestation of the region's resolve to keep markets open; strengthen regional economic integration; support an open, free, fair, inclusive, and rules-based multilateral trading system; and, ultimately, contribute to global post-pandemic recovery efforts. Through new market access commitments and streamlined, modern rules and disciplines that facilitate trade and investment, RCEP promises to deliver new business and employment opportunities, strengthen supply chains in the region, and promote the participation of micro, small and medium enterprises into the regional value chains and production hubs.

It is expected that RCEP will promote trade between the member states through lower tariffs, more flexible ROOs, and standardized customs regulations and procedures. In addition, RCEP will provide for general rules to minimize NTMs, and at the same time, make customs procedures more consistent, thus promoting trade facilitation (Tran Thi Hong Minh, 2021). For ASEAN countries in general and Vietnam in particular, RCEP is not aimed at accessing more markets, but at multi-lateralizing ASEAN+ FTAs, maximizing economic benefits, harmonizing commitments and regulations in existing ASEAN+ FTAs, especially on ROOs and trade facilitation, and thus facilitating the consolidation of regional supply chains and post COVID-19 economic recovery (MoIT, 2021).

Compared to EVFTA and CPTPP, provisions of RCEP on ROOs for garment and textile are more flexible. RCEP allows cumulation of raw materials from all 15 signatory countries while

CPTPP is “Yarn forward” and EVFTA is “Fabric forward”. Therefore, Vietnam’s garment and textile businesses will have more opportunities to expand markets as it is easier to meet ROOs requirements. Accordingly, RCEP allows cumulation of raw materials originating in the whole block. Vietnamese businesses thus can use raw materials from both ASEAN countries and their partners including Australia, New Zealand, Japan, China, and South Korea. Under this rule, products are regarded originating if meeting one of three conditions: products wholly obtained in one member country; products made from raw materials originating in one or more member countries; products made from non-originating raw materials but meeting requirements of product-specific rules.

In addition to cumulation of raw materials, businesses might choose to apply for certificate of origin (C/O) at authorized agencies like before, issue the C/O or declare C/O by themselves if meeting requirements under the agreement. This flexible C/O rule will help reduce transaction costs, saving time, and facilitating Vietnam’s garment and textile exports to potential markets like Japan. Previously, under Vietnam-Japan FTA (VJFTA) and ASEAN-Japan FTA (AJCEP), to enjoy preferential tariff treatments, Vietnam’s garment and textile products must use fabrics originating in ASEAN or Japan while the CMT process must be done in Vietnam. Only few Vietnamese businesses can meet this ROOs requirement since a large proportion of raw materials are imported from China. Meanwhile, under RCEP, regardless origin of raw materials, Vietnam’s garment and textile exports to Japan still enjoy preferential tariff treatment as long as the CMT process is done in Vietnam. Therefore, this new ROOs provision will open up opportunities for more Vietnamese garment and textile products to enter Japanese market.

In addition, Vietnamese garment and textile businesses will also benefit from RCEP’s commitments on trade facilitation, improving market access, promoting trade in goods and trade in services, simplifying customs procedures, harmonizing ROOs within ASEAN and signatory countries including China. This will open up new opportunities for Vietnamese garment and textile businesses to enter and expand market share in this huge market.

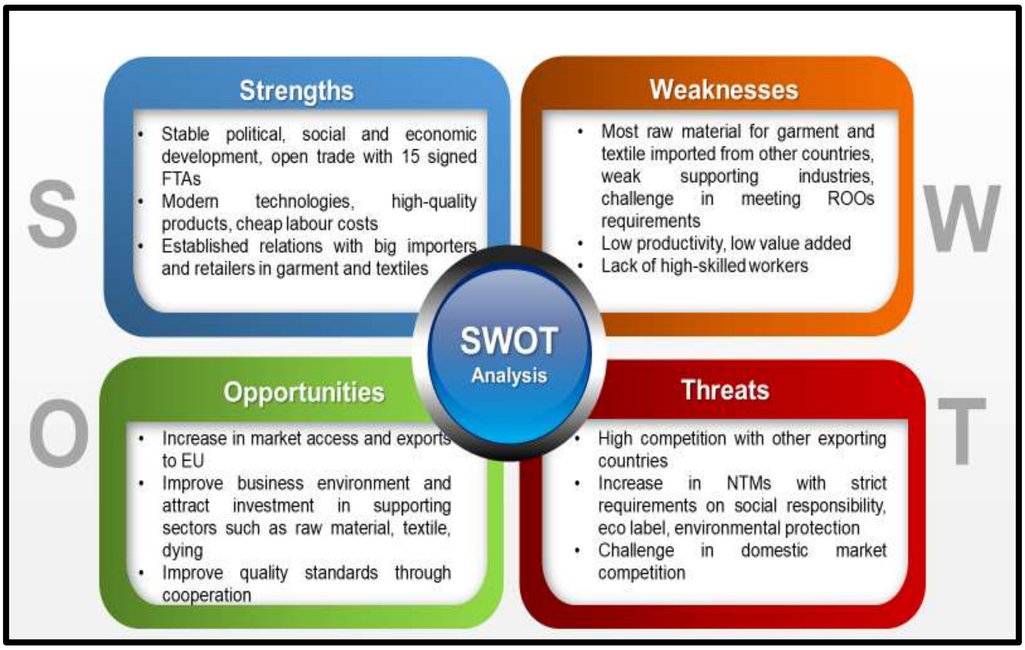
3. Opportunities and challenges from EVFTA’s NTMs for Vietnam’s garment and textile exports: a SWOT analysis

To understand opportunities and challenges from EVFTA in general and EVFTA’s NTMs for Vietnam’s garment and textile exports, in-depth interviews were conducted with senior experts from ministries, research institutes, garment and textile businesses and business associations including MoIT, the Vietnam Chamber of Commerce and Industry (VCCI), the Vietnam Textile and Apparel Association (VITAS), the Central Institute for Economic Management (CIEM), and the Research Centre for Employment Relations (ERC).

In addition, a group discussion using the SWOT approach was conducted with representatives from garment and textile companies as part of a workshop on responsible business conduct and the apparel and footwear industry organized by VCCI in April 2021 including Garment 10 Corporation, Phong Thai Corporation, Fair Wear Foundation, Hoang Duong Textile

Group, Phuong Thao Garment Ltd., Thai Tuan Garment and Textile Ltd., 19-5 Textile Company, Thanh Tri Import Export Garment Company, and 10/10 Textile Company. Figure 3 summarizes opportunities and challenges for Vietnam garment and textile exports from EVFTA's NTMs as shared by experts and businesses in in-depth interviews and group discussions.

Figure 3: SWOT analysis of opportunities and challenges for Vietnam garment and textile exports from EVFTA's NTMs



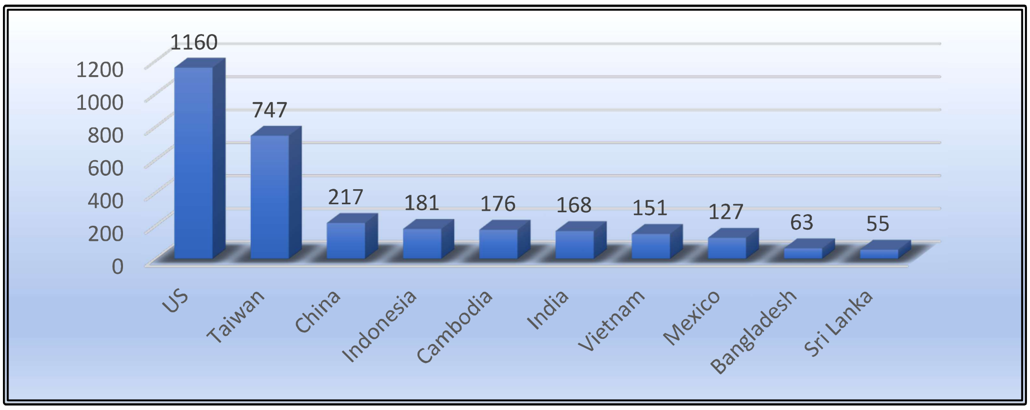
3.1. Strengths

Thanks to Vietnam's political stability, rapid social and economic development, and trade openness, Vietnam's garment and textile export is expanding market shares in the world market, even to demanding markets like the EU, US, and Japan. Equipment is modernized with new technologies while quality product is improving. At the same time, Vietnamese garment and textile businesses have developed long-term partnerships with international importers and retailers.

According to statistics of VITAS, Vietnam has around 6000 businesses in garment and textile, of which 85% work in apparel processing and 15% work in textile. Compared with four biggest competitors, including China, India, Indonesia, Bangladesh, Vietnam has competitive advantages in terms of low labor costs, preferential treatments under EVFTA and CPTPP, experiences in producing high-value products, low-price diesel and electricity, and good infrastructures.

In terms of labour advantage, Vietnam's workers have good skills and are quick at learning new techniques and requirements, even for high-quality products. The average salary of workers in garment and textile industry in Vietnam is among the lowest countries in the world. As shown in Figure 4, the average monthly salary of Vietnam's garment and textile workers is around USD 151, lower than main competitors in the region like India, Cambodia, Indonesia, or China.

Figure 4: Average monthly salary of garment and textile workers in some countries, USD/month



Source: VITAS (2021).

Compared to main competitors in the region who are still struggling to control effects of COVID-19, Vietnam's garment and textile businesses area are gradually back to normal operation thanks to enormous efforts of Vietnamese government in implementation of vaccination campaigns in 2021.

3.2. Weaknesses

A large proportion of Vietnamese garment and textile products are exported in the lower tiers of the value chain, mostly under the Cut-Make-Trim (CMT) or the Original Equipment Manufacturing (OEM) processes. Pattern and fashion designing is not developed while productivity is still low. Meanwhile, textile and supporting industries have not developed to meet demands of high-quality raw materials of the garment industry. As a result, added value of Vietnamese garment products is still low due to high dependence on imported raw materials.

As most of Vietnamese garment and textile businesses are small- and medium- size, it is difficult for them to mobilize capital for production expansion and modernization of equipment and technologies. Therefore, the economy of scale is still limited. Also, due to small scale of production, most of Vietnamese garment and textile businesses are only capable to export to certain markets.

On the other hand, most of Vietnamese garment and textile businesses do not have long-term business strategies. Due to limited capacity in marketing and promotion, they are not capable to wider introduce products to potential customers. Low production management skills and lack of high-skilled workers are also common weaknesses of Vietnamese garment and textile businesses.

3.3. Opportunities

As textile and garment production is moving from developed countries to developing countries, including Vietnam, garment and textile businesses have opportunities to get access to capital, advanced equipment and technologies, management experiences transferred from developed countries. In addition, as Vietnam is increasingly integrating into the world's economy, Vietnamese garment and textile businesses have better access to international markets, especially after Vietnam became WTO member in 2007 and subsequently joined several bilateral and multilateral FTAs.

In-depth interviews with the experts confirm that Vietnam's garment and textile industry enjoys a lot of benefits from EVFTA. Luong Hoang Thai, Director General of the Multilateral Trade Policy Department of MoIT thinks that EVFTA has created opportunities for Vietnam's garment and textile industry as 77% of tariff lines were eliminated to 0% as soon as the agreement became into force. Meanwhile, EU is the largest importer of garment and textile products in the world with total annual import value of more than USD 100 billion. EU is also one of the biggest markets of Vietnam's garment and textile exports.

Agreeing with Thai's viewpoint, Nguyen Thi Thu Trang, Director of Centre for WTO, and International Trade under VCCI also believes the EU is an attractive potential market for Vietnam's garment and textile exports. Although the absolute value of Vietnam's garment and textile exports to the EU is relatively high at USD 3.08 billion in 2020, it only accounts for more than 2% of the total imported garment and textile products to the EU. This means the EU market space is still huge.

After one year of implementation, EVFTA has contributed to increase of bilateral trade between Vietnam and EU. This is especially important as the economy is facing challenges caused by COVID-19 pandemic. According to Nguyen Anh Duong, Head of Research Division at the Central Institute for Economic Management (CIEM), EVFTA creates more favorable conditions for Vietnamese businesses including garment and textile to increase export to the EU market. As one of two countries in Southeast Asia signed FTA with the EU, Vietnam has more competitive advantages in exporting to this market.

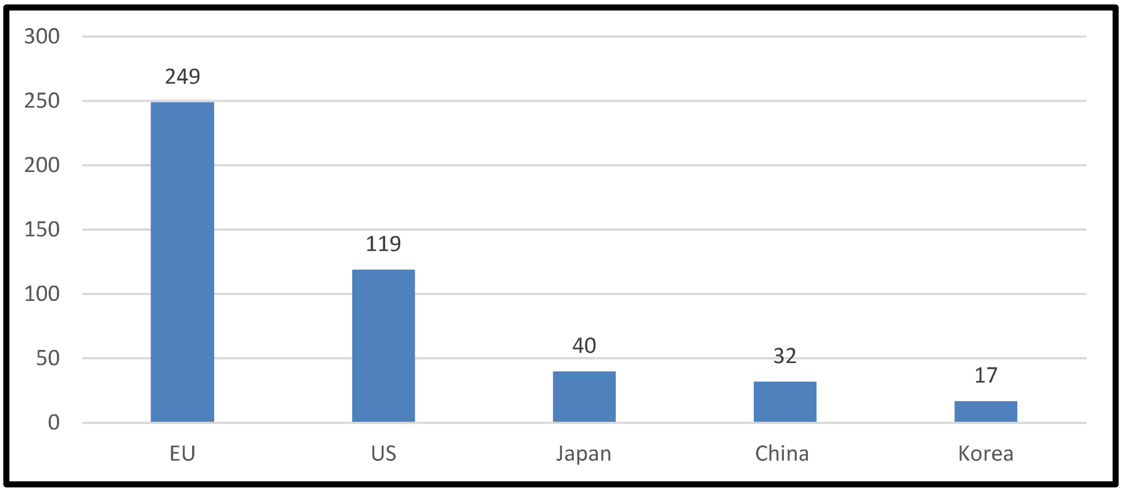
While requirements on ROOs under EVFTA have created the biggest challenge to Vietnam garment and textile businesses in terms of raw materials as analyzed in the following section, they might also create opportunities for Vietnam to attract domestic and international investors in textile and dyeing industry, the bottleneck in raw material supply in Vietnam. To take advantage of these opportunities, the government should issue strategies to encourage investment in this area. In practice, as shared by Vu Duc Giang, President of VITAS, EVFTA and other new FTAs signed by Vietnam have created incentives for FDI flow shifting into Vietnam in textile and garment accessories. Presently, investors from Europe and US have implemented big projects on wool spinning plants in Da Lat and weaving projects in Binh Dinh and Nam Dinh. In addition, investors from Russia and the Middle East are investing in million-dollar projects on garment accessories, textile, dyeing. This is a good opportunity for Vietnam to not only attract FDI but also upgrade to modern and environmental-friendly technologies in these supporting industries.

As COVID-19 situation is still complicated in many countries with the new Omicron variant, Vietnam's garment and textile exports have opportunities to increase export value to meet high demand in personal protective equipment, especially masks and protective clothes. In addition, while demand on normal garment and textile products is declining, EU consumers tend to buy more sport clothes for exercises as they are more aware of importance of heath to fight against COVID-19 and other diseases. This is a good opportunity for Vietnamese garment and textile businesses to diversify types of products and expand the market.

While the 4th wave of COVID-19 pandemic has caused severe damages to the garment and textile industry in Vietnam, recent developments, including re-opening of garment and textile companies since October 2021, high vaccination rates of workers, and increase in imported raw materials have confirmed rapid recovery of the industry. This is a good sign for Vietnam's garment and textile exports in 2022 and 2023 when demand of international market is expected to bounce back after a long period of lock down.

It is forecast that demands of five largest exporting countries of Vietnam's garment and textile products in 2022 will be back to the same value of 2019 before COVID-19 pandemic occurred as shown in Figure 5 below.

Figure 5: Forecast of demands of 5 largest exporting countries of Vietnam's garment and textile products in 2022, USD billion



Source: VITAS (2021).

3.4. Threats

Like other industries, Vietnamese garment and textile industry is also facing typical challenges in economic integration as an immature player from developing countries in the world's export market. These challenges come from weaknesses analyzed above, including low starting point of the industry, low capacity of supporting industries, dependence on imported raw materials, high percentage of processing products, low competition capacity, *etc*. While legal and regulatory framework reforms have considerably facilitated production and export of garment and textile products, there are still gaps in enforcement of these policies, resulting in obstacles for businesses.

EVFTA has put the Vietnam's garment and textile industry under high pressure for reforms. As shared by Mr. Luong Hoang Thai, EU is a demanding market. When developing trade relationship with a country, the EU not only pays attention to trade aspects but also looks at reform efforts to assess determination of that country in economic development towards sustainable development. Meanwhile, in the past, Vietnam's garment and textile industry used to focus on expanding business scale to create more jobs without paying attention to long-term strategies and sustainable development. As competition is increasing globally, investment might be transferred from one country to another easily. Therefore, it is important for Vietnam's garment and textile industry to establish sustainable supply chains to meet expectations of the EU.

As tariff barriers are substantially removed as part of global trade liberalization, countries tend to apply more and more sophisticated NTMs especially requirements on TBTs, SPSs, environmental, social, and governance (ESG) criteria to protect domestic production. Vietnamese businesses, especially small and medium size enterprises find it harder and harder to meet those requirements to enter and expand market shares. At the same time, Vietnamese garment and textile businesses are also facing high competition from other exporting countries, especially from developing countries having similar comparative advantage of low labor costs.

Results of group discussions with garment and textile companies also confirm one of the biggest challenges of EVFTA's NTMs to Vietnamese garment and textile exports is meeting ROOs requirements to enter the EU market. While the rule on cumulation of origin allows Vietnam to use raw materials from Korea as a flexible measure for enjoying preferential treatment under EVFTA, it is still a difficult math to solve for Vietnamese garment and textile businesses, especially in terms of price competition as South Korean fabrics and yarns often have higher prices than those imported from China and Taiwan. Meanwhile, the price competition is more and more fierce. If Vietnam does not have a long-term competition strategy, it is very difficult to retain in the EU market. Therefore, Vietnamese garment and textile businesses should develop long term strategies to change from price competition to non-price competition through capacity improvement, diversification of products focusing on high-quality products.

The challenge in raw material supply is not just a challenge on ensuring stable domestic inputs for the garment and textile industry without dependence on imported sources but also a challenge on how to take advantage of preferential tariff treatments from EVFTA. Despite great efforts, 90% of raw materials for Vietnam's garment and textile industry are imported from non-signatory countries and thus do not meet the rule on cumulation of origin to enjoy preferential treatments under EVFTA.

To solve the issue of shortage of raw materials to meet ROOs requirements in EVFTA, Vu Duc Giang, President of VITAS proposes the Government and local authorities to have strategies to develop industrial zones specialized in textile and dyeing. These strategies should create incentives to attract foreign investment in raw materials and accessories for garment and textile industry.

EVFTA's commitments on environmental protection is another big challenge to Vietnamese garment and textile businesses in general and the textile sector in particular. In order to develop sustainably in the long term, it is crucial that the industry applies solutions to improve technologies to minimize effects of toxic chemicals discharged from textile operations into the environment. In addition, energy efficiency should be ensured during production.

Although it is forecast that demand on garment and textile in international market will rebound from 2022 onward, Vietnam's garment and textile exports might face several challenges including high freight, price competition disadvantage caused by exchange rate volatility, and labor shortage as a result of 4^{th} wave of COVID-19 pandemic.

4. Conclusion and policy recommendations

Our research results confirm that Vietnam's garment and textile exports have a lot of opportunities to expand its EU market share over the next few years. Preferential tariff treatments under EVFTA have strengthened the comparative advantage of Vietnam's garment and textile exports compared to main competitors with similar conditions in the region. In the first year of EVFTA enforcement, despite adverse effects of COVID-19 pandemic, export value of Vietnam's garment and textile products to the EU still saw an increase in 2021 compared to the previous year. While the absolute value of Vietnam's garment and textile exports to the EU is relatively high over the last few years, it only accounts for 2-3% of the total import value of the whole EU market. Therefore, Vietnam's garment and textile businesses should take advantage of EVFTA's preferential treatments to increase the market space.

However, Vietnam garment and textile industry still has weaknesses as an immature player in the world's export market, including low starting point, low capacity of supporting industries, overreliance on imported raw materials, high percentage of processing products, low competition capacity, and lack of long-term business strategies. Meanwhile, EVFTA has put the Vietnam's garment and textile industry under high pressure for reforms to meet expectations of the EU high standards on NTMs especially requirements on TBTs, SPSs, environmental, social, and governance (ESG) criteria. To address these challenges, it is recommended that the Government and businesses should take appropriate actions as follows.

- *For the Government*

It is recommended that the Government of Vietnam implement following measures to further strengthen legal framework and business environment to facilitate exports of Vietnamese goods including textile and garment products to the EU market.

First, the Government should continue reforming institutional and policy framework for implementation of international commitments especially new-generation FTAs like EVFTA, increasing effective mobilization of investment capital, improving business environment, revising FDI policies to attract investors and projects meeting requirements of Vietnam's development, and encouraging responsible business practices for sustainable development.

Second, while improving legal and policy framework in compliance with international commitments, the Government should pay attention to ensuring consistency and stability of business environment without affecting benefits of businesses and investors by timely revising and amending provisions of national laws in line with commitments in bilateral, regional and multi-national agreements that Vietnam is a signatory.

Third, administrative reform is further strengthened in all areas, especially investment, construction, land, taxation, customs, import and export to meet requirements of economic integration. Business licensing and application of business conditions should be strictly monitored. In addition, consistency and transparency of financial institutions should be improved to meet practical requirements of social-economic development.

Fourth, dissemination and communication activities on commitments of FTAs joined by Vietnam should be promoted to increase awareness of sectors and industries, local authorities, businesses and the people. Trade policies should be improved to meet practical conditions of Vietnam and requirements of FTAs signed or being negotiated by Vietnam.

Fifth, strategies on long-term capacity building to increase competitive advantage for Vietnamese industries and sectors including textile and garment should be developed to meet requirements of FTAs, especially high demanding markets like EU. Presently, the MoIT is drafting a strategy on development of the garment, textile, and footwear industries from 2021 to 2030 with a vision to 2035. The strategy should specify directions on investment in development of raw material production to meet ROOs requirements in new-generation FTAs, facilitating localization of raw materials, encouraging changes from processing to higher value-added processes in the value chain, promoting trademarks based on advanced technologies, improving quality assurance, protection of labor rights and environment in compliance with international standards.

- *For Vietnamese businesses*

As analyzed in the previous chapter, EVFTA creates opportunities for Vietnamese businesses to enter and expand market share in the European market. At the same time, the agreement also increases pressure for Vietnamese businesses to improve competitiveness through reform of production technologies, strengthening capacity and productivity, meeting international standards. Therefore, it is recommended that Vietnamese businesses should take following measures to take advantage of preferential treatments as well as to minimize negative impacts of EVFTA.

First, in the context of increasingly economic integration, Vietnamese garment and textile businesses must develop a new vision for sustainable development. Under this vision, Vietnam's garment and textile exports will have the comparative advantage of high quality, advanced technologies, high productivity, timely delivery, transparency, energy efficiency, and environmental protection commitments instead of just low labor costs like present.

Second, Vietnamese businesses should take collective actions to increase competitiveness and reputation of Vietnamese goods in international markets, especially in demanding markets like the EU. To this end, it is important to develop long-term business strategies, strengthening capacity, improving quality, diversifying products, and developing national trademarks of key export products that Vietnam has comparative advantage. At the same time, to maximise EVFTA's preferential tariff benefits, Vietnamese garment and textile businesses should establish chain links. This will help mitigate adverse effects of market fluctuation, especially slow economic growth rate of the world due to negative impacts of COVID-19 pandemic.

Third, corporate governance should be reformed using advanced information technologies. While improving product quality, businesses should also focus on marketing and promotion activities to increase trademarks and reputation of Vietnamese goods. At the same time, business and product strategies should pay attention to improve competitiveness capacity for Vietnamese goods to compete with goods imported from other countries in the region in both domestic and international markets. As members of ASEAN and other regional forums and associations, Vietnam enjoys great benefits for speeding up economic integration but also faces challenges especially in terms of competition pressure from neighboring countries having similar comparative advantage of cheap labor costs and geographical favorable conditions. Most importantly, businesses should increase awareness on commitments of new-generation FTAs like EVTA to develop an appropriate schedule for adaptation. As mentioned in Section 2 of this study, since tariff barriers are substantially removed under commitments of these FTAs, countries tend to retain NTMs as measures to protect domestic products, especially in the form of complicated and high-standard requirements. Therefore, Vietnamese businesses including garment and textile companies should be prepared to meet these requirements.

Fourth, human resource management should be improved with satisfactory renumerations and benefits to retain experienced employees, especially high-skilled workers. This in the long run will increase competitive advantage for Vietnam in international economic integration. Additionally, it is essential for businesses to reform salary scale based on productivity and business performance, creating incentives for self-improvement of professional skills and knowledge by employees.

Fifth, business associations should increase their role as a bridge between state management agencies and businesses, providing advice on legal and regulatory reform to the Government to improve business environment, increasing awareness and building capacity for businesses to actively engage in economic integration with improved knowledge on trade policies, business laws and commercial dispute resolution. Specifically, training workshops on trade barriers, NTMs, market access should be organized regularly to help Vietnamese businesses to expand market shares at both domestic and international markets.

Finally, Vietnamese businesses should be aware and prepare for dealing with increase in NTMs with strict requirements on social responsibility, ecolabel, and environmental protection. As a labor-intensive industry, Vietnamese garment and textile businesses should also pay attention to meeting requirements on human rights due diligence in the supply chain of EU companies. This is especially important as the EU Parliament just approved an outline proposal for the EU Directive on Mandatory Human Rights, Environmental and Good Governance Due Diligence in March 2021. It is expected this new legislation will be approved by the European Parliament in 2022 with mandatory application from 2023 at the earliest. The draft EU legislation states that the rules apply to companies doing business in the European market. This includes non-European suppliers. Companies must follow the new due diligence rules. This means taking measures to prevent harm to human rights, the environment and good governance. If companies cause harm, they will have to pay a penalty unless they can prove they have acted in line with due diligence. While the new legislation aims to better protect the rights of victims or stakeholders in developing countries including Vietnam, it also means Vietnamese companies must comply with this requirement to enter or retain in the value supply chain of EU firms.

This paper has certain limitations as it was conducted when EVFTA just entered into force for more than one year. Data sources are still insufficient to quantify impacts of EVFTA's NTMs on Vietnam's trade in general and on Vietnam's garment and textile exports in particular. In addition, the COVID-19 pandemic has caused disruption in global supply chain, which severely affects the textile and apparel industry over the last two years. Therefore, it is necessary to conduct more vigorous research in the future to have comprehensive views on long-term effects of EVFTA's NTMs when the global economy is fully recovered.

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