BRIEFING

International Agreements in Progress

EU-Vietnam free trade agreement

OVERVIEW

The free trade agreement (FTA) negotiated in 2015 with Vietnam has been described as the most ambitious deal of its type ever between the EU and a developing country. Not only will it eliminate over 99 % of customs duties on goods, it will also open up Vietnamese services markets to EU companies and strengthen protection of EU investments in the country.

According to European Commission figures, the FTA could boost Vietnam's booming economy by as much as 15 % of GDP, with Vietnamese exports to Europe growing by over one third. For the EU, the agreement is an important stepping stone to a wider trade deal with south-east Asia. However, Vietnamese manufacturing sectors may suffer from competition with the EU. NGOs and the European Parliament have also criticised the Commission for pursuing closer ties with a politically repressive regime, although the deal includes some safeguards against negative outcomes.

Conclusion of the FTA was delayed by a 2017 opinion of the European Court of Justice. The Court ruled that the EU does not have the power to conclude agreements on certain investment-related issues on its own; therefore, the text as it then stood would also have to be ratified by the 28 Member States.

To enable at least some parts of the FTA to be ratified more speedily at EU level, in August 2018 the EU and Vietnam agreed to take provisions on investment, for which Member State ratification is required, out of the main agreement and put them in a separate Investment Protection Agreement (IPA). Both the FTA and IPA are currently in translation and are expected to be formally submitted to the Council in late 2018, possibly enabling the FTA to come into force in the second half of 2019.

Free trade agreement between the European Union and Vietnam

Committee responsible:	International Trade (INTA)
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Introduction

Dynamic growth in EU-Vietnam economic relations

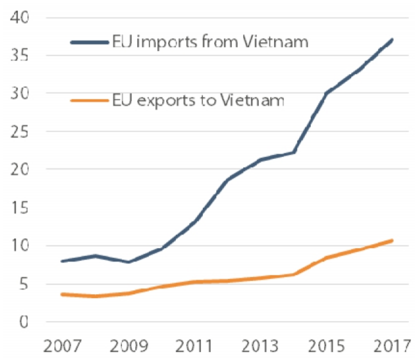
Trade in goods. The balance of trade is heavily in Vietnam's favour, with the EU importing over three times as much from Vietnam as it exports to it. EU-Vietnam imports and exports have grown at double-digit rates, quadrupling over the past ten years to reach a total value of €47.6 billion in 2017. The EU is Vietnam's third-largest trading partner, while Vietnam is the EU's 19th largest partner in the world (second largest in south-east Asia after Singapore). Vietnam exports electronic equipment (such as mobile phones and computers) to the EU, together with shoes, garments and vegetable products; the EU exports machinery, cars and chemicals (including pharmaceutical products) to Vietnam.

Trade in services totalled €3.6 billion in 2016, with a slight balance (€198 million) in the EU's favour.

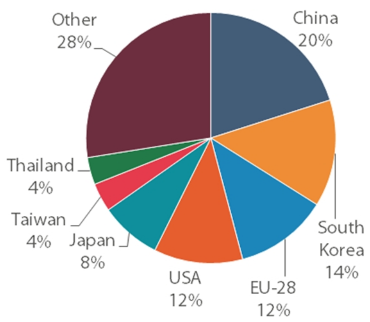
The EU is not only a key trading partner for Vietnam, but also its largest non-Asian investor: in 2016, the EU invested US$1.5 billion in Vietnam, bringing its accumulated investment in the country up to US$8.3 billion.

Figure 1 – EU-Vietnam trade – facts and figures

EU-Vietnam trade in goods
(€ billion)



Vietnam main trading partners
(% total trade in goods, 2017)



€37.0 billion
EU imports from Vietnam

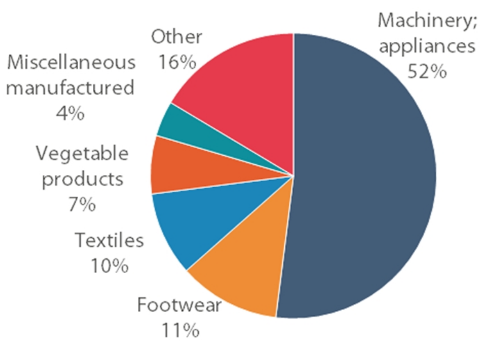
€10.6 billion
EU exports to Vietnam

€47.6 billion
total EU-Vietnam trade

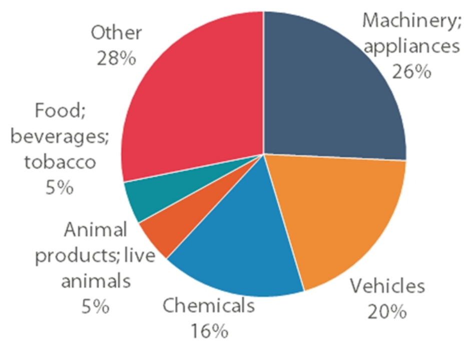
1.3%
as share of total EU external trade

19th
Vietnam's rank as EU trading partner

Main EU imports from Vietnam (2017)



Main EU exports to Vietnam (2017)



Average rates of import duties (from world, trade weighted average MFN tariff applied, 2015)

Vietnam: **5.6 %**; European Union: **3.0 %**

Data source: European Commission, DG Trade (2017), World Trade Organization (2017).

Both sides benefit from trade and investment ties

The agreement aims to stimulate trade and remove many of the remaining barriers to investment. For EU companies, Vietnam is a highly attractive place to do business, not just as a competitive production base with low labour costs and access to the dynamic south-east Asian region, but also as a rapidly growing market for EU exports. Vietnam will also benefit, as trade and investment fuel continued economic growth (which has averaged [6 %]() over the past ten years), bringing the country closer to its [target]() of becoming an advanced industrialised economy.

Flourishing economic relations tarnished by human rights and sustainability concerns

Despite the obvious economic benefits of a free trade agreement with Vietnam, many stakeholders have expressed reservations due to human rights concerns. Political change in Vietnam has not kept pace with economic development. The country remains a one-party state where no dissent is tolerated. It has some of the least free media in the world (ranked 175th out of 180 countries in the 2018 Reporters Without Borders Press Freedom Index). In 2018, Vietnamese courts continued to hand down harsh jail sentences to journalists, bloggers and activists who challenge the Communist Party's grip on power. Independent trade unions are not allowed and there are few laws to protect labour rights.

Economic development has put the environment under pressure. For example, in April 2016 toxic discharge from a steel plant caused possibly irreversible damage to sea life; illegal trade in rare animals continues, despite a recent crackdown.

How the free trade agreement fits with broader EU/Vietnam policies

Both the EU and Vietnam see free trade agreements as a means of tapping into the potential of trade to boost economic growth. For the EU, the Vietnam FTA is part of an ambitious agenda of trade talks with partners from all over the world, including Singapore, the Philippines and Indonesia. For the European Commission, the ultimate goal in south-east Asia is a region-to-region FTA with all ten ASEAN (Association of Southeast Asian Nations) countries; a deal with Vietnam (the EU's second largest trading partner in the region) would be an important step in this direction.

Heavily dependent on external trade (which in 2017 represented a massive 190 % of its GDP), Vietnam is equally eager to conclude free trade deals. It has already signed no fewer than

11 preferential trade agreements, including six as a member of ASEAN, as well as bilateral FTAs with Japan, Korea, Chile and the Eurasian Economic Union. Such deals also help Vietnam reduce its dependence on China, an issue of particular urgency in the context of the territorial dispute between the two countries in the South China Sea. An FTA with the EU is all the more important for Hanoi, now that the United States (which accounts for 20 % of Vietnam's exports, compared to the EU's 19 %) has pulled out of the Trans-Pacific Partnership, which Vietnam had hoped to benefit from.

Existing situation

As a member of the World Trade Organization since 2007, Vietnam has committed itself among other things to lowering customs duties, removing some of the inequalities between foreign and domestic investors, opening up its services markets (much more so than its south-east Asian neighbours) and implementing the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). It has made considerable progress towards meeting these commitments – for example, non-weighted average rates of customs duties fell from 18.5 % in 2007 to 9.6 % in 2017, although concerns remain, for example in the field of intellectual property protection.

For trade in goods, Vietnam already enjoys preferential access to European markets under the EU's Generalised Scheme of Preferences. Under these arrangements, the country is exempt from duty on over half (53 %) of its exports to the EU, and pays an average weighted duty on the remainder of just 4.2 % (however, as this is non-reciprocal, EU exports to Vietnam do not benefit from reduced customs duties). In the absence of a free trade agreement with the EU, Vietnam will lose this preferential access three years after its per capita gross national income (GNI) exceeds the World Bank threshold for upper-middle-income countries (currently US$3 896); even if rapid economic growth continues, this will not happen till around 2030, given that the country's current per capita GNI is just over half of the threshold.

In 2012, Vietnam also signed a Partnership and Cooperation Agreement (PCA) with the EU, which came into force in October 2016. It envisages closer cooperation on a wide range of areas including energy, migration and human rights. There is a link between the PCA and FTA: if Vietnam fails to meet its obligations under the PCA (for example, respecting human rights and democracy, Article 1 PCA), the FTA can be suspended (Articles X.17(2) FTA, 57 PCA).

Parliament's position

The text of the free trade agreement, agreed in 2015, follows many of the Parliament's recommendations in its April 2014 resolution, for example: fair competition between European and Vietnamese companies; protection for intellectual property and foreign investments; a binding sustainable development chapter; and a clause that allows the EU to suspend the FTA if there are severe human rights abuses in Vietnam.

However, the EP's position remains divided. The resolution of 17 December 2015 welcomes the conclusion of the PCA and FTA, but it and further resolutions on Vietnam (June 2016 and December 2017) point out serious human rights concerns. In September 2018, a cross-party group of 32 MEPs sent a letter to EU Trade Commissioner, Cecilia Malmström, and EU High Representative, Federica Mogherini, urging them to insist on improvements to the human rights situation in Vietnam, before the FTA can be concluded. It remains to be seen whether such concerns will significantly affect the Parliament's willingness to consent to the conclusion of the agreement.

Vietnam is currently drawing up a new Labour Code. Although this is unlikely to bring major changes, such as allowing independent trade unions as required by core ILO conventions (which Vietnam has committed to ratifying in the FTA), improvements could go some way to meeting EP concerns about Vietnamese labour rights.

The INTA committee is due to hold a hearing on the FTA on 10 October 2018.

Preparation of the agreement

European Commission impact assessments. In 2009, shortly before talks on an FTA between the EU and ASEAN as a whole broke off, the Commission produced a trade sustainability impact assessment on a region-to-region agreement. According to this, Vietnam would be by far the biggest beneficiary of all ASEAN countries, with a predicted surge of 35 % in exports, 15 % in GDP and 13 % in salaries For its part, the EU was expected only to gain 0.2 % GDP and 1 % additional exports from an EU-ASEAN FTA. While these figures are several years old, a more recent study (in 2015, of predicted benefits from the Trans-Pacific Partnership) reached similar conclusions, suggesting that Vietnam remains one of the best-placed Asian countries to benefit from free trade deals.

Based on the 2009 impact assessment, a 2013 Commission document analyses the likely effects of a bilateral FTA in greater detail (only on Vietnam; the impact on the EU is not discussed). According to this, the Vietnamese textiles, footwear and leather sectors would be the main winners. Despite the overall gains for Vietnam, some sectors could lose out: cereals and grains, motor vehicles, electronics, machinery and insurance. By boosting economic activity, the FTA could indirectly aggravate environmental problems, resulting in more emissions, increased deforestation and more widespread overfishing. The Commission therefore recommends gradual phasing in of lower customs duties to allow for structural adjustments in the Vietnamese economy, together with an ambitious sustainability chapter. Both recommendations have been followed in the FTA.

The European Commission is currently working on a detailed analysis of the FTA's expected economic impact both on Vietnam and the EU, expected later in 2018.

The above documents do not look at human rights aspects, however. In 2014, the European Parliament and the European Ombudsman recommended that the Commission carry out a separate human rights impact assessment. The Commission responded with a document discussing the FTA's human rights and sustainability implications.

Finally, in line with its usual practice, the Commission plans to carry out an *ex post* economic, social and environmental impact assessment of the FTA. The starting date is yet to be decided, but based on past experience, it will probably be around five years after entry into force of the FTA, once there are enough data to measure the effects.

Negotiation process and outcome

- **2007**: the EU launches talks on a region-to-region free trade agreement with ASEAN.
- **2009**: due to lack of progress, the EU decides to suspend talks with ASEAN and negotiate with individual south-east Asian countries instead.
- **June 2012-August 2015**: after 14 negotiation rounds, agreement on broad lines of FTA.
- **2 December 2015**: negotiations on FTA concluded.
- **August 2018**: to speed up the ratification process (see below), the EU and Vietnam agree to split the agreement into an FTA and a separate Investment Protection Agreement.

The changes the agreement would bring

According to the European Commission, the Vietnam FTA is the most ambitious free trade deal ever concluded with a developing country. Its main features are:

Almost complete elimination of customs duties. The FTA will eliminate over 99 % of customs duties in both directions:

- EU exports to Vietnam: 65 % of duties to disappear as soon as the FTA enters into force, and the remainder to be phased out gradually over a period of up to 10 years (for example, to protect the Vietnamese motor sector from European competition, duties on cars will remain for the full 10 years);

- Vietnamese exports to the EU: 71 % of duties to disappear on entry into force, the remainder to be phased out over a period of up to seven years.

To qualify for exemption from customs duties, goods must originate in Vietnam or the EU. The FTA includes detailed rules defining the origin of goods which include components from other countries. For example, Vietnamese garments are eligible if the fabric from which they are made is woven in Vietnam, the EU or Korea (which has FTAs with both Vietnam and the EU) — even if the yarn used to weave the fabric comes from another country altogether. This is quite a generous provision as many FTAs only exempt garments from duty if both the fabric and yarn originate from a given country.

Reduction of non-tariff barriers. As well as customs duties (tariffs), there are many non-tariff barriers to trade with Vietnam, for example differing technical standards and complex customs procedures. The FTA will reduce some of these obstacles: Vietnam will align more closely with international standards on motor vehicles (UNECE Vehicle Regulations which the EU already applies) and pharmaceuticals. As a result, EU manufacturers will be able to export cars and other motor vehicles without them having to undergo Vietnamese testing and certification procedures. In addition, Vietnam will simplify and standardise customs procedures.

Access to Vietnamese public procurement. The FTA will allow EU companies to bid for Vietnamese government contracts, and vice-versa. This includes contracts with European and Vietnamese national and regional authorities.

Improved access to Vietnamese service markets. The FTA will make it easier for EU companies to provide services in Vietnam, for example in the postal, banking, insurance, maritime transport and environmental sectors.

Investment access and protection. The FTA will open up various Vietnamese manufacturing sectors to EU investment, for example food and beverages, tyres, ceramics and construction materials. EU investors in Vietnam and Vietnamese investors in the EU will have the same treatment as their domestic counterparts. The Investment Protection Agreement accompanying the FTA establishes an investor-state tribunal to resolve disputes between EU investors and Vietnamese authorities (and vice-versa).

Promoting sustainable development. In response to labour rights and environmental concerns about Vietnam, the FTA includes commitments to implement International Labour Organization core standards (for instance, on freedom to join independent trade unions and on banning child labour) and UN conventions (for instance, on combatting climate change and protecting biodiversity).

Intellectual property, state-owned enterprises, geographical indications. To meet EU concerns in these areas, the FTA includes provisions guaranteeing: protection of EU exports from counterfeit goods; fair competition between foreign companies and subsidised Vietnamese state-owned enterprises; protection of 169 EU geographical indications (for example Scotch whisky and Grana Padano cheese).

Stakeholders' views

Both the European Commission and the European Parliament have held public meetings to discuss the EU-Vietnam FTA. Most participants in these events welcomed the FTA, but there were also criticisms.

Business representatives, such as BusinessEurope, are enthusiastic about the FTA's potential to boost trade and investment opportunities. They warn that, unless the FTA is concluded quickly, European businesses will be at a disadvantage compared to competitors such as China which already have FTAs with Hanoi. Business representatives also note that the FTA will not end all the problems faced by EU companies operating in Vietnam, such as the country's non-transparent and inconsistent implementation of legislation.

NGOs are highly critical of the FTA. In June 2018, a total of 90 human rights groups insisted that it would be a 'disgrace' for the EU to conclude an agreement with a country which is one of the 'worst enemies' of human rights. On top of these human rights concerns, Action Aid also argues that the FTA will be bad for the Vietnamese economy, as it will expose Vietnamese manufacturing sectors to European competition.

In addition, Action Aid criticises the investor-state tribunal to be set up to rule on disputes between EU investors and the Vietnamese government. It claims that this tribunal would enable foreign investors in Vietnam to bypass Vietnamese courts and challenge government actions that, albeit having a legitimate purpose (for example, environmental protection), adversely affect their business interests. The risk of expensive legal disputes could deter the government from taking such actions.

However, the European Commission defends the tribunal, arguing that the FTA reaffirms the right of governments to 'achieve legitimate policy objectives, such as the protection of public health, safety, environment or public morals'; companies may only use the tribunal in narrowly defined cases – for example, when EU investors are targeted by clearly abusive treatment which disadvantages them relative to Vietnamese operators, or their assets are expropriated without adequate compensation. According to the Commission, such protection mechanisms will benefit Vietnam by making it easier to attract foreign investment.

The International Federation for Human Rights feels that the provision to suspend the FTA in the event of severe human rights abuses is useful, but does not sufficiently define the conditions for such suspension. It is also disappointed that no human rights impact assessment will be carried out before the FTA comes into force.

In response to such criticisms, the Commission argues that the EU's overall policy towards Vietnam, including the free trade and partnership and cooperation agreements, is supportive of human rights. For example, in the PCA there is the above-mentioned legal provision allowing the EU to suspend the FTA in the event of serious abuses; the PCA also provides for a human rights dialogue with regular EU-Vietnam meetings – this dialogue already began in 2012, even before the agreement was finalised. Moreover, Vietnamese civil society groups will be consulted on the implementation of the FTA. The EU is also supporting such groups financially, helping them to promote human rights and sustainable development in general, and to monitor the FTA once implemented.

Signature and ratification process

In 2017, initial plans to present the FTA to be signed by the Council during the year were put on hold after a 16 May 2017 opinion of the European Court of Justice on the FTA with Singapore: according to this, non-direct ('portfolio') investment and investor-state dispute settlement mechanisms are shared competences, on which the EU shares decision-making powers with Member States. The opinion meant that the EU-Singapore FTA (and by analogy, similar agreements such as the EU-Vietnam FTA) could not be concluded by the EU alone, given that it includes provisions relating to shared competences, but must also be concluded by all the Member States.

To speed up the ratification process, the EU and Vietnam decided in August 2018 to follow the approach already adopted for the EU-Singapore FTA, and split the original text into two parts, an FTA which includes only exclusive EU competences and can therefore be concluded relatively quickly by the EU alone, and a separate Investment Protection Agreement (IPA). Both texts have now been finalised and sent for translation into EU languages and Vietnamese. The translations are expected to be ready in late 2018 enabling the FTA and IPA to be approved by the Commission and submitted as a package to the Council before the end of the year. As the Council will probably need a few months to discuss the two texts, they are unlikely to reach the Parliament for formal deliberations before spring 2019. In practice this means that Parliament's consent, enabling the FTA to finally come into force, is unlikely before autumn 2019, in the next term. The IPA is likely to take longer, due to the requirement for Member State ratification.

European Parliament supporting analysis

Armanovica M., EU-Vietnam economic and trade relations, Policy Department for External Affairs, European Parliament, September 2012.

Vandewalle L., Mendonca S., Vietnam: despite human rights concerns, a promising partner for the EU in Asia, Policy Department for External Affairs, European Parliament, October 2015.

Other sources

Trade Sustainability Impact Assessment on EU-ASEAN FTA, Annex on Vietnam, European Commission, 2013.

Human Rights and Sustainable Development in EU-Vietnam Relations with specific regard to the EU-Vietnam FTA, European Commission, 2016.

Guide to the EU-Vietnam Free Trade Agreement, European Commission, 2016.

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Third edition. The 'International Agreements in Progress' briefings are updated at key stages throughout the process, from initial discussions through to ratification.

To view earlier editions of this briefing, please see: PE 614.702, February 2018.