



## RMG: Vietnam overtakes Bangladesh but the game is not over

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For starters, this should not have come as a surprise. It was a long-time coming. Vietnam was hot on our heels for almost a decade. Bangladesh trailed China in apparel exports for nearly twenty years, but as a distant second. As a single, country-exporter of apparel, Bangladesh captured 6.5 per cent of the global export market against China's dominant 35 per cent, but dwindling. Vietnam, meanwhile, which had turned into an export powerhouse in the 21st century, was right behind Bangladesh in apparel exports, though it had a much-diversified

export basket. In calendar year 2020, the value of merchandise exports from Vietnam totalled \$ 281 billion, up 6.4 per cent, when world exports declined by 7.8 per cent, and Bangladesh's fell by 17 per cent. Actually, Vietnam's share of global exports rose in the pandemic year 2020 further entrenching its role in global manufacturing-supply chains. Its apparel exports rose to \$29 billion, topping Bangladesh's exports of \$28 billion, to become No.2, after China.

Is this a transient event or a harbinger of bad news for the longer term. To reach any conclusion, it is important to take a closer look. First, Vietnam handled the Covid pandemic remarkably well to keep export-oriented manufacturing humming for much of 2020. Second, Vietnam is by far the major beneficiary of US-China trade tensions that diverted massive FDI inflows away from China into Vietnam at the same time that US consumer demand resumed. Recent trends show that the number of orders shifting from China to Vietnam has seen a significant increase. Consequently, Vietnam's total exports to US grew 26 per cent in 2020 with its share of US imports rising to 2.7 per cent, up from 1.9 per cent in 2017. In particular, Vietnam gained US market share in apparel. Third, Vietnam's growing popularity is the country's collection of free trade agreements (FTAs)-most notably, the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), EU-Vietnam FTA (EVFTA) and RCEP. With a few more bilateral FTAs (e.g. Japan, Australia, New Zealand) Vietnam has attained near zero duty access to over 50 per cent of the world market. It is the combination of FDI and FTAs that makes Vietnam a competitor to be reckoned with over the long term.

However, it is the stark differences between Vietnam and Bangladesh in respect of the structure of their apparel industry and export potential that are worth pondering about. Vietnam's apparel industry is segmented between local producers with little interest in exporting and foreign-invested enterprises that only export. Most domestic textiles are not of export quality, and domestic producers only meet 15 per cent of domestic demand for textiles. As for exports, over 90 per cent comes from firms owned by foreign enterprises who import inputs from their global networks (with minimal local backward linkage) and whose sales are coordinated from headquarter locations abroad. This is true not just for the apparel sector but also for other manufactures such as electronics, computers, mobile phones, footwear, and sundry machinery. Vietnam's exports of electronic goods and mobile phones have seen phenomenal growth in recent years making Vietnam No.2 exporter of mobile phones (about \$50+ billion), after China. Vietnam is also the No.2 exporter of coffee, after

Brazil, but poised to become the No.1 producer and exporter of coffee in the world. In rice exports, Vietnam is No.2, after India. Interestingly, Vietnam, with a richly diversified export basket, ranks among the top two exporters of the world in several products, not just garments. Given recent trends, it is likely to be the top exporter in more than one product.

Textiles and apparel consistently rank among Vietnam's leading export industries. According to Oxford Economics, a leading global forecast and analytics firm located in Oxford, UK, the industry now boasts over 6000 textiles and garments manufacturing companies, employing upwards of 2.5 million workers. The growth of the garment industry has been impressive. It has been fast catching up with Bangladesh over the past 10 years or so. From the data coming out of BGMEA we note that the number of local firms is around 4500, of which some 1000 could be closed or operate intermittently. Data on the number of garment workers in Bangladesh has been hard to get but hovers around 4 million. That alone tells us something about productivity of Vietnamese workers who now produce and export close to what Bangladesh does with 1.5 million fewer workers. Vietnam's investment in education and skill development is apparently paying off in terms of labor productivity.

In the immediate term therefore, it looks like the game is not over. Bangladesh's export recovery is on track with 15 per cent per cent growth in FY2021 and prospects for FY2022 look good in view of solid projected global output and trade growth over the next two years. Reports of rising volume of export orders are coming out from industry leaders. The outlook for calendar year 2021 suggests that Bangladesh apparel exports could be back to pre-pandemic levels of \$33-34 billion which Vietnam is unlikely to catch up in just one year. So Bangladesh could be back as No.2 for another year or two but not for long. Here is why.

In apparel and electronics, Vietnam has pursued an overwhelmingly FDI route without regard to domestic value addition, receiving inflows of \$28 billion (11 per cent of GDP) in 2020. The objective has always been to expand exports and capture world markets thus creating jobs at home. In apparel it imports 85-90 per cent of inputs (i.e. fabrics and accessories) and in case of electronics import share is even more. Domestic value addition in exports is extremely low as evidenced by the fact that exports of \$281 billion in 2020 exceeded Vietnam's GDP of \$260 billion. That happens to highly trade-oriented economies (e.g. Singapore).

Vietnam embraced a strategy of becoming increasingly investor-friendly by offering generous

financial incentives, streamlining business regulations, and improving the quality of its workforce. Since the mid-2000s, the Vietnamese government has offered extremely competitive financial incentives to businesses seeking to set up operations in the country, in addition to a zero per cent withholding tax on dividends remitted overseas and a low corporate income tax (CIT) rate of only 20 per cent. To top it all, FDI regulations called for minimal local content requirement- a typical FDI inhibitor. These advantages have enabled Vietnam to become a premier “sourcing economy” in the eyes of many companies.

In consequence, FDI in Vietnam has not only brought copious amounts of capital but created skill-based jobs, infused innovation, improved management, opened retail windows in developed country markets, upscaled to higher value added apparel (of man-made fiber) and electronic products, and so on. Though domestic spillover effects of such FDI volumes are not reported to be significant so far, it is a matter of time when this will lead to widespread uplift of quality, management and innovation in domestic enterprises. Vietnam appears to be well placed to become even more competitive in the global marketplace over time.

Bangladesh, on the other hand, has an apparel industry that is largely indigenous in ownership and management, except for a small share of foreign-invested enterprises located in EPZ. From the start it has adopted all the right policies to take full advantage of its comparative advantage in this labour-intensive export product and it has succeeded in attaining the No.2 position for a long time. But, to stay ahead of Vietnam in apparel exports, Bangladesh now needs to do two things: first, it has to open up FDI inflows unconditionally into its leading manufacturing sector (RMG), in principle and in practice; second, it must ramp up a number of FTAs by the time LDC graduation comes into force in 2026. Without these two additional ammunitions in its armory, there are signs that Bangladesh could slip into No.3 in the next five years or so.

In closing, I wish to point out that just as Bangladesh is being recognised for its successful experiment in development, Vietnam has given a new twist to the paradigm of export-led growth, a breakthrough development paradigm during the 1970s - the success story of export-led rapid growth demonstrated by East Asian economies. China, under Deng Xiaoping, took note with its switch to trade openness and global integration starting in the 1980s, signaling its own brand of socialism with market orientation - domestic and international. Vietnam soon followed suit with its Doi Moi reforms in 1984 with another variety of market-

oriented socialism that also embraced trade openness and export-led growth, but of a new kind. Instead of the typical East Asian format Vietnam adopted a new version of export-led growth predominantly driven by FDI and bolstered by free-trade market access via multiple FTAs covering the better part (over 50 per cent ) of the global marketplace.

This is unique in the realm of trade policy. What lessons might there be for Bangladesh?

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