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Advancing Free Trade
for Asia-Pacific **Prosperity**

Supporting Industry Promotion Policies in APEC – Case Study on Viet Nam

APEC Policy Support Unit
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EXECUTIVE SUMMARY

- Viet Nam is one of the fast growing emerging economies in Asia. It has moved from low income to lower-middle income status over a short span of 10 years. Its real GDP grew on average 6.1 percent over the last decade, while proportion of people living in extreme poverty fell from about half in the early 1990s to less than 5 percent in 2012 (World Bank World Development Indicators).
- Part of its growth story can be attributed to the progress made in its industrial sector, which includes manufacturing. Collectively, the sector contributed about 33 percent to its GDP in 2015 and made up 21 percent of total employment in 2013. Manufactured goods has made up more than half of its merchandise exports since 2003 and accounted for more than three-quarters of its total merchandise exports as of 2014 (World Bank World Development Indicators).
- Cost matters in the world of manufacturing. In fact, low labour cost has been one of the main reasons for Viet Nam to be successful in attracting FDI, an important contributor to the development of its manufacturing sector.
- With progress and changing global landscape, however, it can no longer rely on low labour cost as the main factor to continue attracting FDI. Additionally, the economy needs to bolster its industrial capability and move up the value chain if it is to sustain its growth and avoid middle income trap.
- One area which the economy can work on is improving the state of its supporting industry, which various sources have shown to be relatively weaker compared to their counterparts in other APEC middle income economies.
- The relatively under-developed state of supporting industry in Viet Nam can be attributed to several reasons, including: 1) lack of resources to make capital investment necessary to manufacture parts and components of the appropriate quality; 2) lack of certifications issued by bodies such as International Organization for Standardization (ISO), resulting in firms being unqualified to be suppliers in certain value chains; 3) high cost of supplied parts and components due to low economies of scale, which is partly due to its small market capacity domestically; 4) inability to respond quickly to changes in demand for parts and components; 5) relatively poorer quality of labour force; 6) firms' hesitation to be pro-active in upgrading and in product development process; and 7) communication barriers with potential customers.
- The government of Viet Nam realizes the importance of developing its supporting industry and has promulgated a number of laws/regulations with implications on supporting industries directly and indirectly. Special attention is paid to small and medium-sized enterprises (SMEs), which makes up approximately 97 percent of firms and are major source of employment and contributor to its economy. Generally, the myriad of policies can be classified under three main headings: 1) policies specifically targeted at supporting industry development; 2) policies to develop SMEs; and 3) policies relating to the general business environment. There are also parallel activities undertaken by organizations other than the government to support the development of supporting industries in Viet Nam.
- The government has undertaken many actions which could be considered good practices. Examples include providing one clear definition of supporting industry; having a wide range of assistance policies and incentives, employing several mechanisms during policy development process (i.e. conducting industry consultations, incorporating inputs from academia as well as studying and

adopting relevant policies and other economies); simplifying application procedures to access incentives; and utilizing various channels to raise firms' awareness of policies.

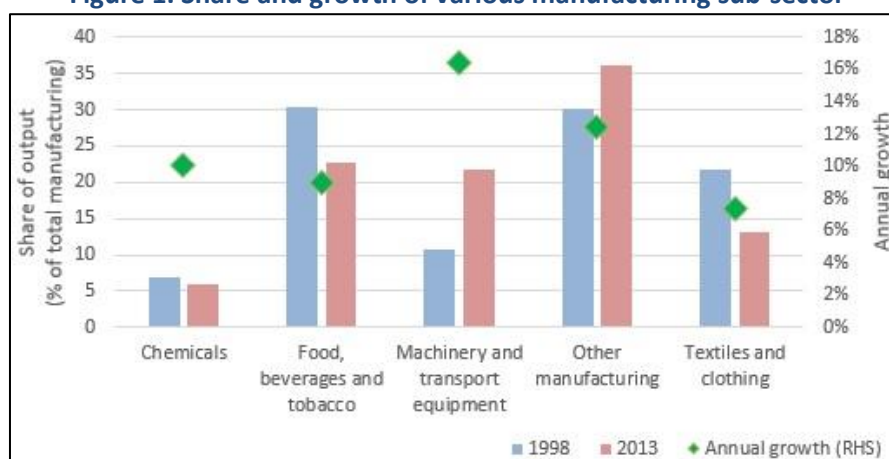
- However, this case study also identifies some areas for further improvements. Examples include re-considering the usefulness of having a list of supporting products which are eligible for incentives; exploring the definition of supporting industries to include services providers; providing more information to clarify the nature of incentives, types of activities covered and mechanisms to access them; further improving the procedures to access the incentives; enhancing the coordination between agencies involved in this endeavour; and reviewing the relationships and resolving any inconsistencies between laws/regulations.
- Addressing these areas of improvements could put Viet Nam in a prime position as it continues to strengthen its supporting industry.

1. ECONOMY PROFILE

Viet Nam is one of the fast growing emerging economies in Asia. Growth of its real gross domestic product (GDP) reached on average 6.1 percent over the last decade¹. Classified as lower-middle income economy under World Bank's definition, Viet Nam's gross national income (GNI) per capita reached US\$1,990 in 2015, nearly tripled that in 2005 (US\$680)². The proportion of people living in extreme poverty fell from around 50 percent in the early 1990s to about 3 percent in 2014.

Part of Viet Nam's growth story can be attributed to the enormous progress made in its industrial sector which includes manufacturing. Collectively, the sector contributes about 33 percent to its GDP in 2015 and made up 21 percent of total employment in 2013. By manufacturing sub-sectors, machinery and transport equipment as well as other manufacturing (which includes electronics) expanded at the fastest rates among all categories (Figure 1).

Figure 1. Share and growth of various manufacturing sub-sector



Source: World Bank and APEC PSU calculations

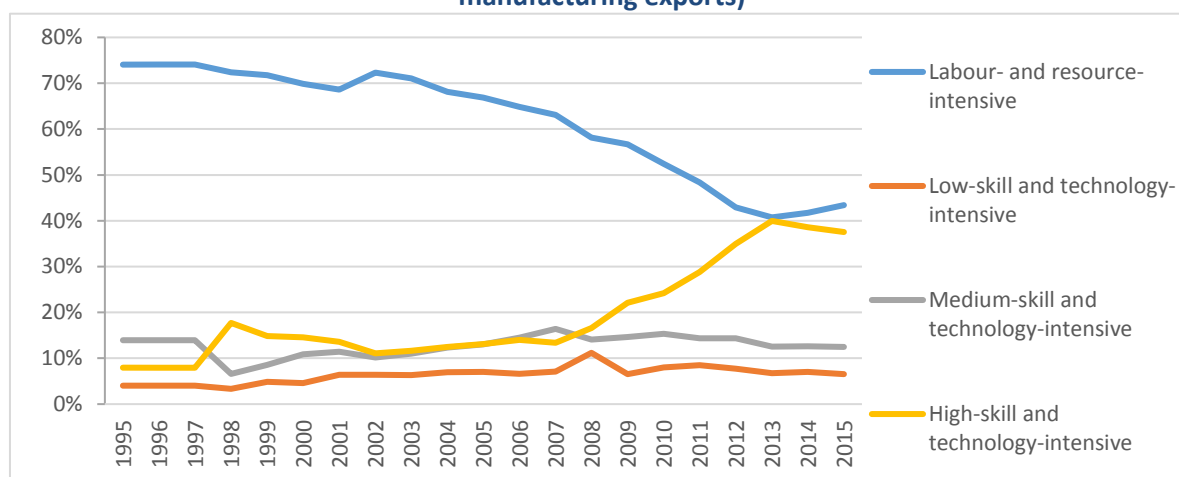
Manufactured goods has contributed to more than half of its merchandise exports since 2003 and accounts for more than three-quarters of its total merchandise exports as of 2014³. Viet Nam has also consciously shifted its focus towards exports of high-technology products since 2000. As seen in Figure 2, the share of labour-intensive and resource-intensive exports fell from 70 percent in 2000 to 43 percent in 2015, while high-skill and technology-intensive exports grew from 15 percent to 38 percent over the same period.

¹ Data is calculated based on annual GDP growth from 2006 to 2015. All data mentioned in the first two paragraphs are obtained from World Bank World Development Indicators.

² Data is based on current USD (Atlas method).

³ Merchandise goods include agricultural raw materials; food; fuel; manufactures; and ores and metals. Data is obtained from World Bank World Development Indicators.

Figure 2. Exports of manufactures by degree of manufacturing (as a percentage of total manufacturing exports)



Source: UNCTAD and APEC PSU calculations

Foreign direct investment (FDI) is an important contributor to its development and overall growth. Between 2004 and 2014, Viet Nam has successfully attracted on average US\$21 billion in total registered capital annually, with an average of approximately 1,250 projects (Figure 3). The foreign-invested sector is estimated to contribute around 18 percent to its GDP, close to a quarter of its total investment and about two-thirds of its total exports⁴.

Moving forward, it is likely that Viet Nam would continue to attract significant amounts of FDI. More than 60 percent of Japanese firms shared that they would expand their operations in the economy when surveyed in 2014 and 2015 (JETRO, 2016). 80 percent of US firms indicated that they would do so in the ASEAN Business Outlook Survey 2016 conducted by AmCham. 55 percent of EU firms expected to increase their investment according to the latest EuroCham Business Climate Index Survey conducted in 3rd quarter of 2016.

Figure 3. Licensed foreign direct investment (FDI) flows in Viet Nam (2004-2014)



Source: General Statistics Office of Viet Nam

⁴ World Bank, Taking Stock – An update on Viet Nam’s Recent Economic Developments, December 2016

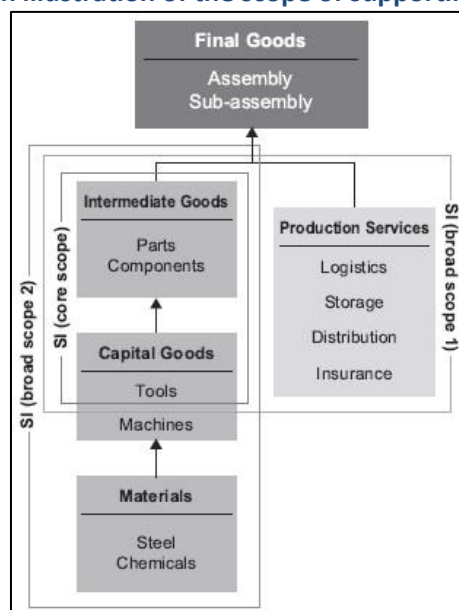
2. SUPPORTING INDUSTRY IN VIET NAM

One of the main draws of Viet Nam to foreign investors is its cost competitiveness, an important factor in the manufacturing industry. Specifically, its low labour cost is highly attractive for firms that are looking at relocating their facilities from other areas where wages have increased. Availability of low cost labour is the highest rated business factor in Viet Nam by investors participating in the ASEAN Business Outlook Survey 2016 conducted by AmCham. In a survey on current situation of Japan enterprises in Asia and Oceania by JETRO, Viet Nam ranks third out of 15 economies in terms of cheaper labour cost.

However, this comparative advantage has been eroding in recent years. Other locations with low labour costs have sprung up, and according to the same JETRO survey, labour costs in Viet Nam's manufacturing sector has increased by 10 percent annually between 2013 and 2015. Depending on the level of staff hired in the manufacturing sector (i.e. workers, engineers or managers), labour cost has increased by 22.5 percent to 110.2 percent between 2010 and 2015. Unless there are other factors that would encourage firms to stay, it is likely that FDI firms would re-consider their investment plans in Viet Nam. It is, therefore, important that Viet Nam stands out among other economies as a prospective FDI destination.

One factor which determines an economy's competitiveness as an FDI destination is the state of its supporting industries, essentially: manufacturers and suppliers of raw materials, capital goods and intermediate goods as well as production services to user firms, which are either assemblers or supporting industry firms themselves (Figure 4). The presence of competent supporting industry firms domestically is a boon to user firms because in theory, they would be able to save on import cost and time. It would also be easier for user firms to monitor their suppliers through regular visits for example. In line with the definition set by Viet Nam in Decree No. 111/2015/ND-CP on development of supporting industry ('Decree 111'), this case study has defined supporting industries as an industry which is involved in manufacturing materials, accessories, components and spare parts used for assembling finished goods (i.e broad scope 2 in Figure 4). Other terms such as "ancillary industries" or "auxiliary industries" are also used to the same effect within Viet Nam.

Figure 4. An illustration of the scope of supporting industries



Note: SI refers to supporting industries

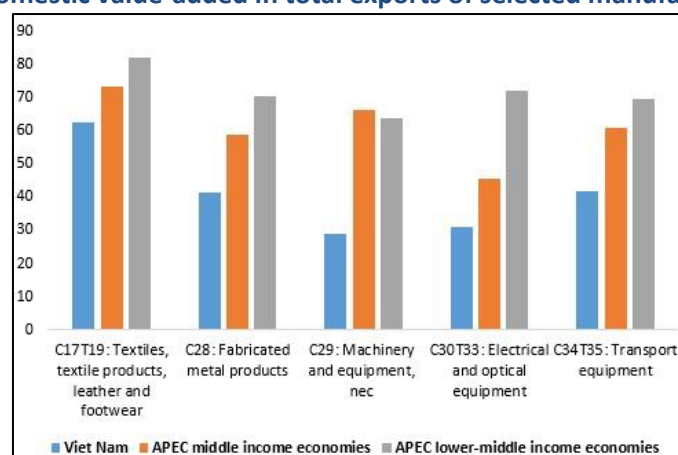
Source: Nguyen, Chapter 2 in Ohno (2007)

Current state of Viet Nam’s supporting industry

Despite the strong performance of its manufacturing sector, as indicated in the previous chapter, there appears to be limited linkages between user firms and supporting industry firms based domestically. Analysis of latest available data (i.e. year 2011) obtained from the OECD Trade in Value-Added (TiVA) database showed that Viet Nam’s domestic value-added share of its total exports for selected manufacturing sectors is generally lower than that of other APEC middle income economies collectively (Figure 5). The same can also be observed when Viet Nam’s share is compared to other APEC lower-middle income economies, which may be more appropriate considering the diverse range of products manufactured by lower-middle and upper-middle income economies⁵.

For example, Viet Nam’s 2011 share of domestic value-added in total exports of electrical and optical equipment was only about 31 percent, while that of other APEC lower-middle income economies were collectively at 72 percent. In the fabricated metal sector, Viet Nam’s share was about 41 percent while that of other APEC lower-middle income economies were collectively at 70 percent. For textiles, Viet Nam’s share of 63 percent was relatively higher compared to its domestic value-added share in other sectors, but this figure was still lower than that of other APEC lower-middle income economies (82 percent).

Figure 5. Share of domestic value-added in total exports of selected manufacturing sectors (2011)

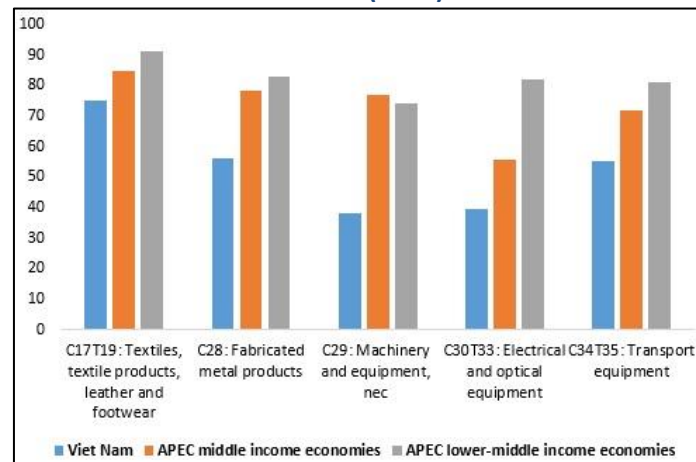


Source: APEC PSU computations from OECD TiVA database. Accessed 26 January 2017

The shares described above have taken into consideration the contribution of services sectors such as logistics and telecommunications to manufacturing. Looking at Viet Nam’s contribution solely from the perspective of manufactures (i.e. raw materials, parts and components and machines) does not change the point that the economy’s domestic value-added shares are relatively lower than that of other comparative economies across all selected sectors (Figure 6).

⁵ Based on World Bank income classification as of December 2016 (<https://datahelpdesk.worldbank.org/knowledgebase/articles/906519-world-bank-country-and-lending-groups>), APEC lower-middle income economies are Indonesia and the Philippines. APEC upper-middle income economies are China; Malaysia; Mexico; Russia; and Thailand.

Figure 6. Share of domestic value-added in exports of manufactures in selected manufacturing sectors (2011)

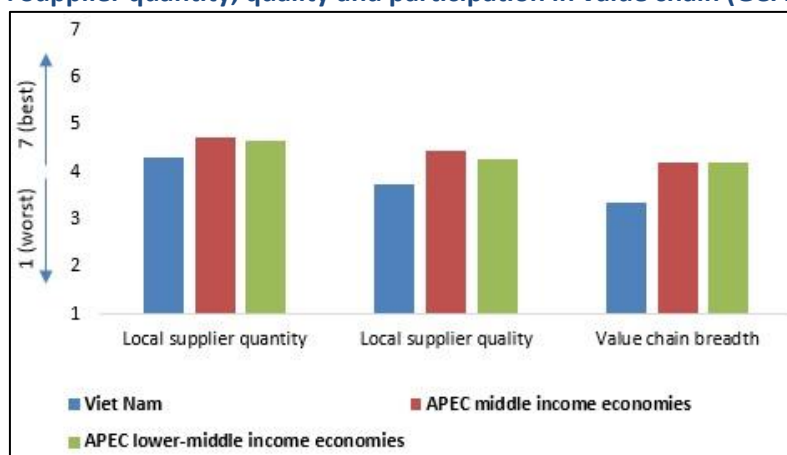


Source: APEC PSU computations from OECD TiVA database. Accessed 26 January 2017

These figures indicated that domestic supporting industries in Viet Nam, at least in the selected sectors, are relatively weak compared to their counterparts in other economies. To complement the above, survey results of Japanese firms operating in Viet Nam showed that difficulty in local procurement of raw materials and parts in the manufacturing sector has consistently been among the top two issues faced by firms in the last two editions of the survey (2014 and 2015). The same survey also indicated that the share of raw materials and components procured locally by survey respondents fell from 33.2 percent in 2014 to 32.1 percent in 2015. In the ASEAN Business Outlook Survey 2016 conducted by AmCham, investor satisfaction level on availability of raw materials in Viet Nam was rated relatively low (19 percent).

Additionally, executive opinion survey conducted by the World Economic Forum for its 2016-17 edition of Global Competitiveness Index showed that both local supplier quantity and quality in Viet Nam are relatively weaker than that of other APEC middle income economies and more specifically, APEC lower-middle income economies (Figure 7). On a scale of 1 to 7 (best), respondents put Viet Nam's score for local supplier quantity and quality at 4.3 and 3.7, respectively. In contrast, the scores of APEC lower-middle income economies excluding Viet Nam are 4.7 (for local supplier quantity) and 4.5 (for local supplier quality). One implication of these scores is that firms' participation in the value chain in Viet Nam is relatively lower compared to their counterparts in other APEC lower-middle income economies (3.3 vs. 4.2).

Figure 7. Supplier quantity, quality and participation in value chain (GCI 2016-17)⁶



Source: APEC PSU computations from World Economic Forum Global Competitiveness Index dataset
Accessed 2 February 2017

The information provided below, which are sector-specific and obtained from various sources including interviews with different stakeholders⁷, validated these observations.

Automotive

Viet Nam’s automotive industry started earnestly in the early 1990s with two FDI firms, namely Mekong Auto and Vietnam Motors Corporation. Since then, the number of firms engaged in the industry as suppliers and assemblers have increased exponentially. Familiar FDI firms include Toyota, Honda and Ford, while domestic firms include Truong Hai and Xuan Kien (PricewaterhouseCoopers, 2006).

The presence of these firms has allowed Viet Nam to develop its automotive industry. However, it is worthwhile to note that localization of automotive parts and components has remained relatively low at 10 to 40 percent depending on manufacturers and type of vehicles (i.e. passenger cars, trucks or buses) (Nguyen et al, 2016). An interviewee noted that while it had tried to increase the number of parts and components procured domestically over the last 5 years, it had not been able to do so successfully because potential suppliers generally were not able to meet its requirements across five areas, namely safety, quality, cost, engineering and management. Another interviewee which manufactures plastic-based components for automotive firms indicated that majority of its raw materials were imported.

Furthermore, localized parts and components are usually low-value goods such as wire harness and tires whose labour cost made up a significant share of its production cost. They also include bulky parts such as seats and batteries whose import cost would be greater than that produced domestically.

Electronics

The development of Viet Nam’s electronics industry started sometime after 2010 as manufacturers looked for more competitive production locations. Besides competitive wages, Viet Nam’s close proximity to China (where the existing supply chains were based), its population size and a growing

⁶ The questions that were asked by World Economic Forum on: 1) local supplier quantity: “In your economy, how numerous are local suppliers? (1= largely nonexistent; 7= extremely numerous); 2) local supplier quality: “In your economy, how do you assess the quality of local suppliers? (1= extremely poor quality; 7= extremely high quality); 3) value chain breadth: “In your economy, how broad is companies’ presence in the value chain? (1= narrow, primarily involved in individual steps of the value chain (e.g. resource extraction or production); 7= broad, present across the entire value chain (e.g. including production, marketing, distribution, design, etc.)).

⁷ The list of interviewees is available in Table 6 in the Annex.

middle class also added to its attractiveness as an FDI destination. Since then, electronics firms such as Intel, LG, Panasonic and Samsung have established their presence in the economy (DBS, 2015).

Despite its high export growth rate and electronics being Viet Nam's top export since 2013, an article by Vietrade (2015) indicated that domestic value-added in the industry remains generally low as most parts and components have to be imported. As an example, the same article noted that only 10 percent of Samsung's suppliers are domestic firms and they provide relatively lower-value added activities such as packing and printing. Another article (Greene, 2014) observed that most facilities set up by electronics firms focus on low-value production and assembly work. Yet another article (BDG, 2016) mentioned that although FDI firms would like to procure locally and have set ambitious target in some cases, the reality has usually fallen short. For instance, Intel indicated in 2014 that it would endeavor to have 80 percent localization rate but the real figure, though not publicly made available, is apparently lower. Fuji Xerox would like to have 90 percent rate over the next few years but have only managed to achieve the current share of 50 percent.

An interviewee which is involved in the printed circuit boards (PCB) value chain shared that as a supporting industry firm, it needs inputs too and despite attempts to increase the number of its local suppliers, it has not been able to identify suitable suppliers for electronics parts. It also gave the example of trying to find local supplier for metal stamping activity but eventually had to engage FDI firm to undertake the activity. At the moment, it only has local suppliers for lower value items such as plastics and packaging materials.

Fabricated metal and machinery & equipment

Machineries, together with dies and molds, are some of the critical inputs for manufacturing, particularly in the automotive and electronics sectors. Dies, for example, are needed to shape metal in stamping and forging activities. Molds are required to shape plastics, ceramics and composite materials among others.

Despite the importance of machinery, dies and molds, it appears that such domestically-supplied parts are not able to compete with imported ones. For example, machinery and technologies in the supporting industry came mostly from other economies such as China; Japan; Korea; and Chinese Taipei, rather than Viet Nam itself (CBI, 2014). An interviewee shared that it mainly supplies steel structures because its other products, such as parts for machine and cutting tools, are not competitive. The interviewee also mentioned that while the firm tried to obtain inputs domestically as a first option, it was often unable to find the right suppliers.

Textiles, garment, leather and footwear

Textiles, garment, leather and footwear are among the traditional sectors in which Viet Nam's competitiveness is well-known globally. According to a publication by CNV International (2016), Viet Nam is the fifth largest garment exporting economy in the world. In terms of footwear exports, Viet Nam is ranked fourth after China, India and Brazil (VnExpress International, 2016).

Despite this, it is worthwhile to note that of all the firms in the textiles industry, only close to 2 percent are involved in spinning activity and only approximately 8 percent are involved in all three activities (i.e. weaving/knitting, dyeing/finishing, and fabric manufacturing). Pertaining to the garment industry, 70 percent are involved in labour-intensive process of CMT (cut, make, trim) whereby input materials such as textiles are supplied by the buyers to the firms. Only about 25 percent are involved in some form of FOB (Freight-on-Board) process which could include procurement of materials and development of sourcing strategies. Even fewer share (i.e. 4 percent) are also involved in design activities (MRI and IPSI, 2016). Furthermore, significant share of cotton and fiber are likely to be

imported since cotton cultivation and fiber production processes in Viet Nam are under-developed, hence making their price non-competitive (FPT Securities, 2014).

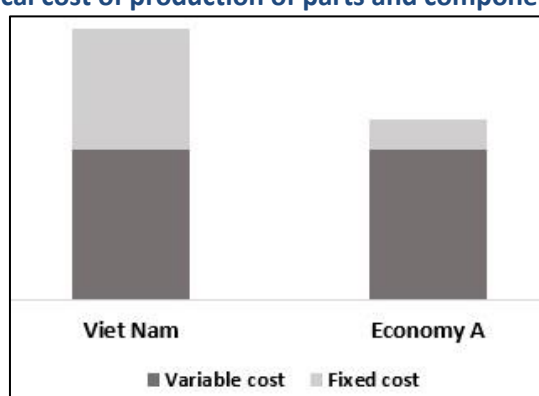
The situation is fairly similar in the leather and footwear industry. 70 percent of firms based in Viet Nam are focused on labour intensive activities such as cutting and sewing. Few are involved in more upstream activities such as raw and intermediate materials production. As a result, user firms generally have to import most of these materials including leather and canvas. An interviewee from an industry association shared that of its 800-plus members, majority are only involved in turning processed leather into shoes, the last step of the value chain for footwear manufacturing. None are involved in raw materials production, only a handful are involved in intermediate materials production, while two are involved in capital goods production.

Reasons for the current state of supporting industry in Viet Nam

The relatively under-developed state of Viet Nam's supporting industry can be attributed to several reasons. For a start, supplier firms are generally unable to meet the QCD (quality, cost, delivery) requirements of user firms and this can be associated to various factors. Firstly, supplier firms lack the resources to make capital investment which are necessary to manufacture parts and components of the appropriate quality. Even if supplier firms can meet the quality set by user firms with existing technology, many may not have the certifications such as those issued by International Organization for Standardization (ISO)⁸ and Automotive Industry Action Group (AIAG)⁹ (in the case of suppliers to automotive assembler firms) and therefore, are not eligible to be qualified as suppliers. In fact, some automotive assembler firms have their own additional standards which potential suppliers need to meet. In addition to the cost of getting certified which may be significant for some firms, certain certification needs to be renewed at regular intervals.

The cost of parts and components supplied by firms also tend to be higher than imported ones and this can mostly be associated to Viet Nam's low economies of scale, which is due partly to its small domestic market. In order to manufacture certain specialized parts, a firm has to make fixed investment in the form of new machineries for example. The relatively low demand for such parts means that firms have to spread the investment cost over smaller number of parts, hence increasing the unit cost and making it less competitive compared to imported parts (Figure 8).

Figure 8. Local cost of production of parts and components (per unit)



Source: Authors' understanding from interviews

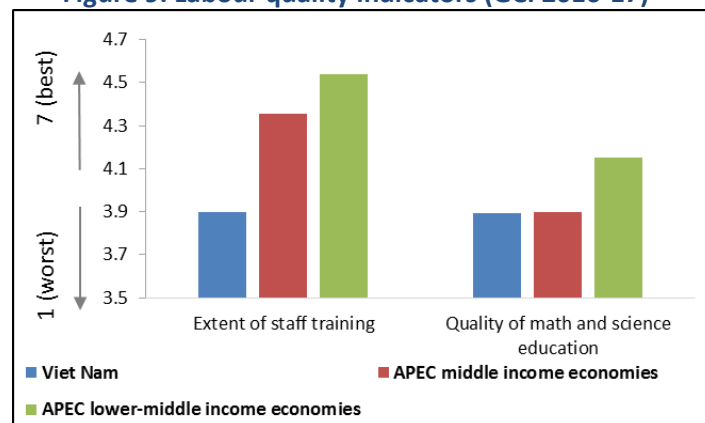
⁸ Example of an ISO certification is ISO/TS16949 which defines the quality management system requirements for the design and development, production and, when relevant, installation and service of automotive-related products. More details can be obtained at: http://www.iso.org/iso/catalogue_detail?csnumber=52844

⁹ Example of an AIAG certification is CQI-11 Plating System Assessment program which is designed to ensure firm's adherence to plating procedures and systems. More details can be obtained at: <http://cqi-support.com/cqi-standards/cqi-11>

Being able to respond to changes in the demand for parts and components along the value chain is very critical to ensure its continuity. In this regard, it is observed that supporting industries in Viet Nam are generally inflexible when it comes to delivery timeline. Furthermore, supplier firms may not have the capacity to increase production even if they want to.

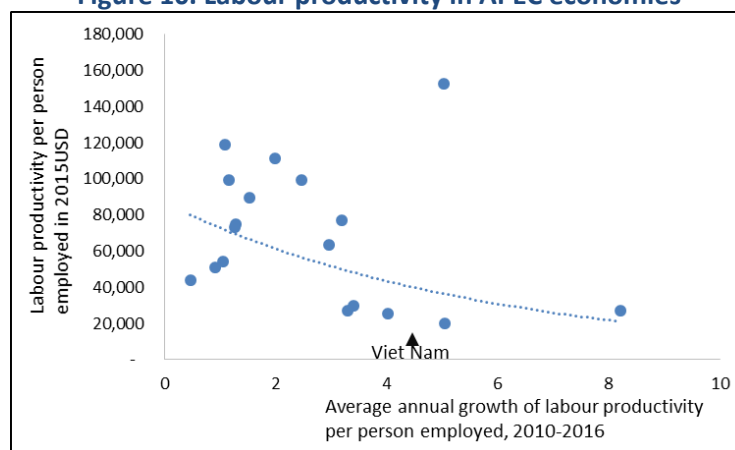
Moreover, Viet Nam’s labour force inadvertently limit the opportunities and prospects of its supporting industry. As shown in Figure 9, the quality of education (in mathematics and science) in Viet Nam is rated lower than that of other APEC middle income economies. Furthermore, companies in Viet Nam do not provide much training and development opportunities. As a result, labour productivity growth has lagged behind other APEC economies (Figure 10).

Figure 9. Labour quality indicators (GCI 2016-17)¹⁰



Source: PSU computations from World Economic Forum Global Competitiveness Index dataset Accessed 13 February 2017

Figure 10. Labour productivity in APEC economies



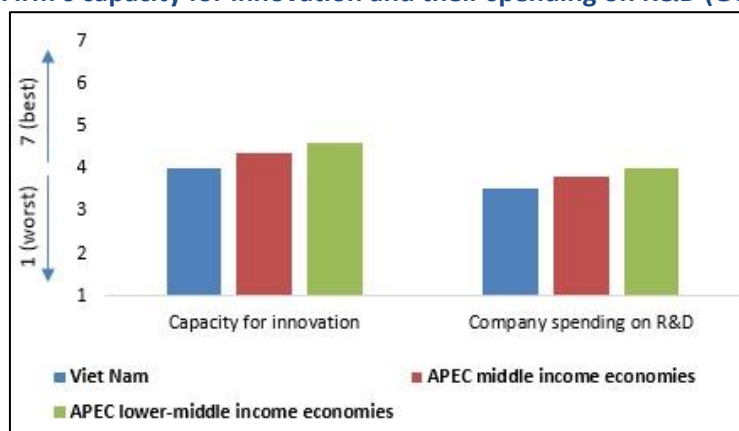
Source: PSU computations from The Conference Board Database. Accessed 12 February 2017

An interviewee from the leather and footwear industry gave an example of supporting industry firms in Chinese Taipei that have the ability to develop new materials through R&D and can therefore take a pro-active approach in engaging user firms, which may lead to large orders if user firms decide to use the materials. This observation is supported by findings from the World Economic Forum, which

¹⁰ The questions that were asked by World Economic Forum on: 1) extent of staff training: “In your economy, to what extent do companies invest in training and employee development?” (1= not at all; 7= to a great extent); and 2) quality of math and science education: “In your economy, how do you assess the quality of math and science education?” (1= extremely poor – among the worst in the world; 7= excellent – among the best in the world).

showed that firms’ capacity for innovation as well as their spending on R&D are lower in Viet Nam than in other APEC lower-middle income economies (Figure 11).

Figure 11. Firm’s capacity for innovation and their spending on R&D (GCI 2016-17)¹¹



Source: PSU computations from World Economic Forum Global Competitiveness Index dataset
 Accessed 2 February 2017

Related to the above is the unwillingness of firms in Viet Nam to actively upgrade their product development and manufacturing process. From the perspective of many firms, such activities are resource intensive, time-consuming, and may not yield the expected return-on-investments. On the other hand, lower-value activities require less resources and bring returns within a shorter timeframe. Firms’ reluctance to innovate can also be due to the perceptions that user firms established in Viet Nam prefer to replicate their value chain with their preferred suppliers. Therefore, it would be challenging for domestic firms to join their value chains.

Furthermore, many firms face language barriers in communicating with their counterparts in the user firms, which most likely are FDI firms. For instance, an interviewee from a foreign industry association noted that Japanese FDI firms prefer to establish supplier relationships with Japanese-speaking firms so as to minimize miscommunication.

Implications of the current state and the importance of developing its supporting industry

The current state of supporting industries in Viet Nam may possibly diminish its attractiveness as an FDI destination, especially since the strength of supporting industries is a significant factor in the decision to invest in the manufacturing industry. While low labour cost could have been the main consideration of foreign investors for deciding to invest, the plethora of other locations with low labour costs, and the fact that wages increase as an economy develops, mean that foreign investors also look at other factors such as the price and quality of parts and components produced by supporting industries.

In addition, the development of supporting industries can bolster the industrial capability of the economy and potentially increase the opportunities available to firms (CIEM, 2016). For instance, supporting industry firms could export their products directly instead of just supplying them to FDI firms locally, thereby further enhancing Viet Nam’s export and growth potentials.

¹¹ The questions that were asked by World Economic Forum on: 1) capacity for innovation: “In your economy, to what extent do companies have the capacity to innovate? (1= not at all; 7= to a great extent); and 2) company spending on R&D: “In your economy, to what extent do companies invest in R&D? (1= do not invest at all in R&D; 7= invest heavily in R&D).

In its Socio-economic Development Strategy (SEDS) 2011-2020, Viet Nam indicated that it would endeavor to achieve an annual GDP growth rate of 7 to 8 percent and an average GDP per capita in real terms of US\$3,000. One possible way to attain these goals would be to continue developing its supporting industries. This is indeed acknowledged in the SEDS 2011-2020 itself, particularly in section IV on ‘orientation in development, innovation of growth model, and restructuring of the economy’. In fact, the SEDS alluded to the types of policies that Viet Nam is likely to implement or continue doing in its bid to further enhance its supporting industries. Examples include “develop reasonable mechanism and policies that assist economic organizations to cooperate in training and improving staff, expanding their market, applying new technology and getting access to capital”, “provide support to strong development of small and medium sized enterprises”, and “promote the effectiveness of industrial cluster and zones”¹².

The development of supporting industries can also help an economy to avoid the middle income trap, as highlighted by Ohno (2010). Under SEDS 2001-2010, Viet Nam has had many significant achievements. It had moved from low income status in 2001 to lower-middle income status in 2010 (according to World Bank income classification) and its economy had been growing at an average rate of 7.3 percent annually. While this is certainly laudable, the paper noted that past achievements have been made possible by lower hanging fruits such as systemic transition to market economy and global integration. Now that these processes are more or less towards completion, Viet Nam needs to be looking at areas such as moving up the value chain to sustain growth to avert the middle income trap. This means continuing its efforts to develop its supporting industries through productivity enhancement, skills improvements and technology adoption among others.

The link between SMEs and supporting industries

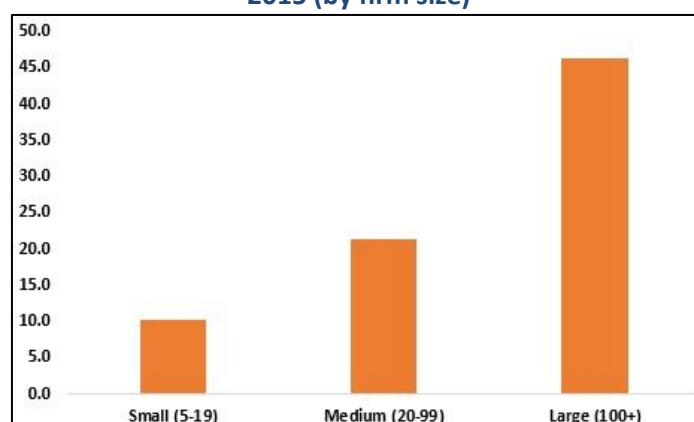
SMEs made up approximately 97 percent of the firms in Viet Nam. They are also major source of employment and contributor to Viet Nam’s economy. Despite their notable shares by these measures, the extent of their participation in the global value chains (GVCs), possibly as supporting industry firms, remains relatively low compared to their larger counterparts. As seen from Figure 12, while close to half of large firms surveyed by World Bank in Viet Nam for its Enterprise Surveys indicated that they export at least 1 percent of their sales either directly or indirectly, the share fell to about 10 and 20 percent for small and medium-sized firms, respectively^{13,14}.

¹² Information in this section is based on the unofficial translation of Viet Nam’s SEDS 2011-2020 obtained from: <http://www.economica.vn/portals/0/maubieu/1d3f7ee0400e42152bdcaa439bf62686.pdf>

¹³ Note that World Bank has excluded firms with fewer than 5 employees from the Enterprise Surveys. While this has led to the absence of insights from this specific group of firms, specifically micro-sized firms, analysis in this section is still generally applicable.

¹⁴ Note that there are differences in how SMEs are defined by the Vietnamese government and World Bank Enterprise Surveys. In the case of Vietnamese government, SMEs are defined by total capital and number of employees which may vary between sector. Generally, firms with less than 300 employees and total capital of less than VND 100 billion can be considered as SMEs. In the case of World Bank enterprise survey, firms with between 5 and 19 employees (inclusive) are considered as small firms, firms with between 20 and 99 employees (inclusive) are considered as medium firms, while firms with 100 employees or more are considered as large firms. Thus, insights on SMEs from the World Bank enterprise surveys are only reflective of certain segments of Vietnamese SMEs (i.e those with less than 100 employees).

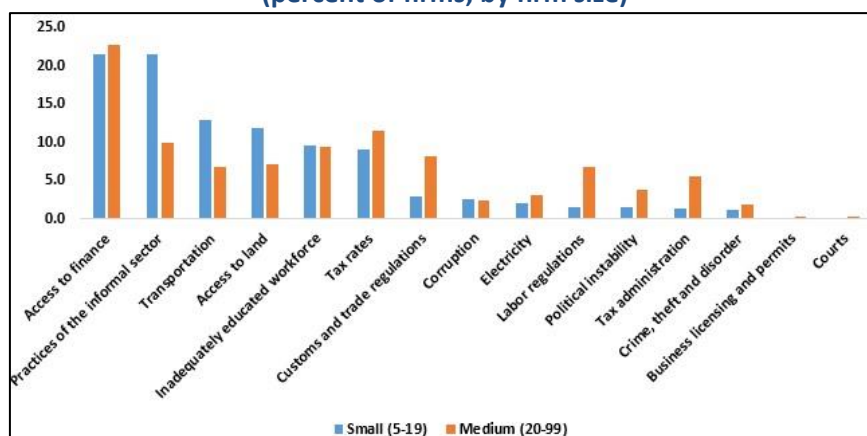
Figure 12. Percent of firms directly or indirectly exporting at least 1 percent of sales in Viet Nam in 2015 (by firm size)



Source: World Bank Enterprise Surveys

While SMEs usually choose to focus on the domestic market, a look at the obstacles identified by firms to be affecting their business operations could provide some additional reasons. At the top of list of obstacles identified by both small and medium-sized firms is access to finance (Figure 13). Financial resources are required for many of firms’ planned undertaking such as expanding capacity, purchasing additional assets, getting international certification, hiring more people as well as sending them for training. Lack of resources means that firms may have to shelve these plans, some of which are critical to become an integral part of GVCs.

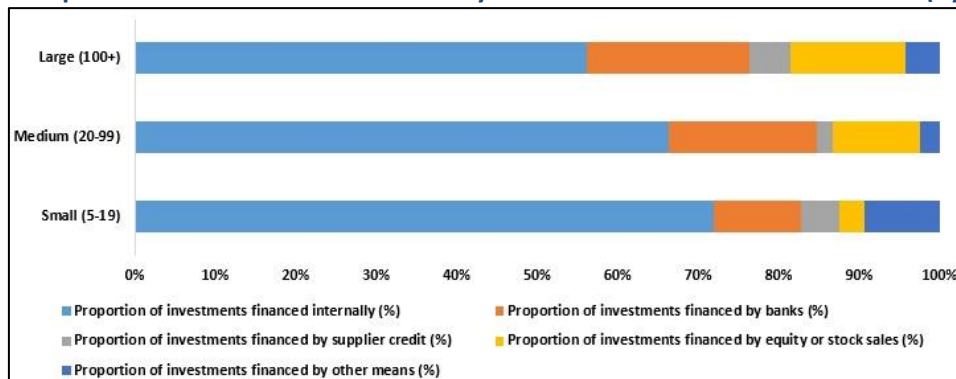
Figure 13. Top obstacles in Viet Nam affecting their business operations in 2015 (percent of firms; by firm size)



Source: World Bank Enterprise Surveys

Figure 14 shows that small firms internally financed a larger proportion of their investments compared to large firms, highlighting that small firms are unable to access credit from external sources such as banks. It is also worthwhile to note that the proportion of investments financed by banks, equity or stock sales appears to be correlated to the size of the firms, meaning small firms have smaller proportion of investments financed by these means compared to medium-sized firms, which in turn have smaller proportion relative to large firms.

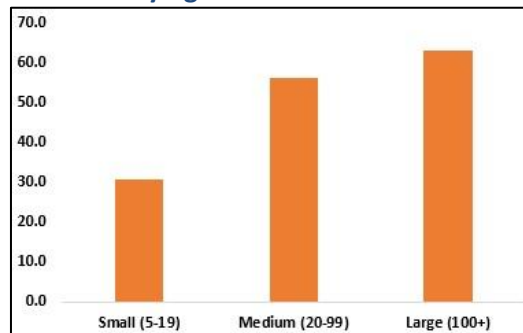
Figure 14. Proportion of investments financed by various means in Viet Nam in 2015 (by firm size)



Source: World Bank Enterprise Surveys

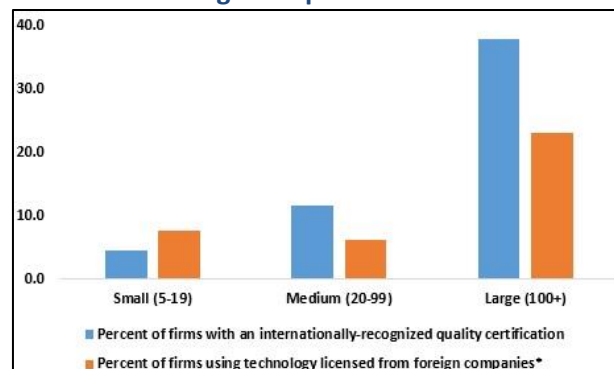
The possible implications of lack of access to finance can be observed through some of the figures below. For example, Figure 15 shows that the share of small and medium-sized firms buying fixed assets is relatively lower than that of large firms. The same pattern can be observed for Figure 16, which shows the share of firms with internationally-recognized quality certification and those using technology licensed from foreign companies. In addition, Figure 17 reveals that relatively fewer small and medium firms offered formal training to their workers compared to large firms.

Figure 15. Percent of firms buying fixed assets in Viet Nam in 2015 (by firm size)



Source: World Bank Enterprise Surveys

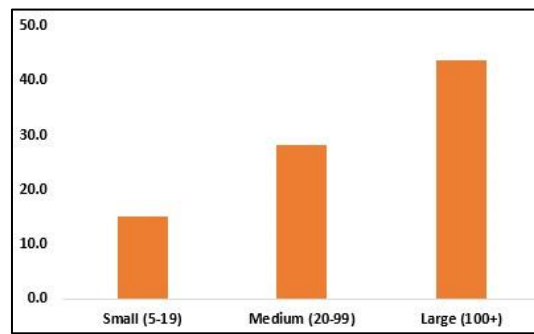
Figure 16. Percent of firms with an internationally-recognized quality certification and those using technology licensed from foreign companies in Viet Nam in 2015 (by firm size)



Note: *This is calculated only for the manufacturing sector

Source: World Bank Enterprise Surveys

Figure 17. Percent of firms offering formal training in Viet Nam in 2015 (by firm size)



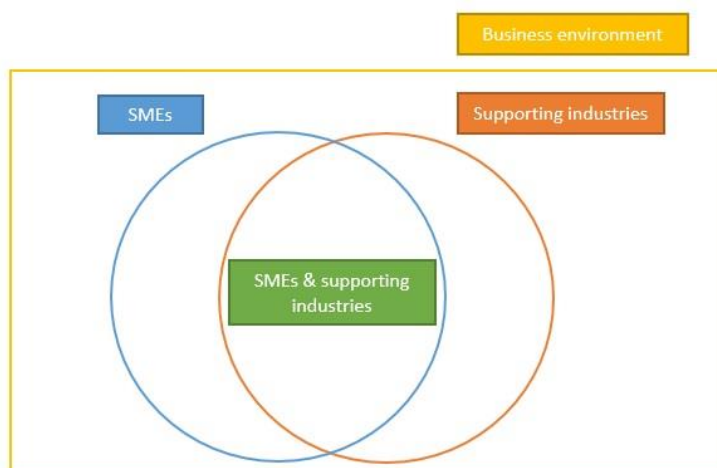
Source: World Bank Enterprise Surveys

Given these, it is important that any efforts at developing supporting industries should specifically target the obstacles faced by SMEs and enable them to deepen their participation as supporting industries.

3. POLICIES FOR DEVELOPMENT OF SUPPORTING INDUSTRIES IN VIET NAM

The term ‘supporting industries’ as mentioned in this case study has been present in Viet Nam since the mid-1980s, although it was only used officially in the 2003 at the beginning of the Viet Nam-Japan Joint Initiative (Nguyen, 2007). Since then, there have been a number of laws/regulations to develop Viet Nam’s supporting industries, both directly and indirectly. In general, the myriad of policies can be classified under three main headings: 1) policies specifically targeted at supporting industry development; 2) policies to develop small and medium enterprises (SMEs); and 3) policies relating to the general business environment (Figure 18). SMEs are of particular interest because as indicated earlier, they made up about 97 percent of firms in the economy and most businesses in supporting industries are small businesses, although it should be made clear that not all SMEs are supporting industries, and vice-versa. Similarly, policies that lead to a conducive business environment, although not specifically targeting supporting industries, are critical for the development of firms in supporting industries.

Figure 18. Categorization of policies and an illustration of their relationships



Source: Authors

This paper will focus on recent policy initiatives for several reasons: 1) they generally have consolidated or built on past legislation; 2) they reflect the government’s current thinking on supporting industry development in the economy; and 3) they allow for more in-depth analysis of these policies given the time and resource constraints. To ensure that the findings of this case study are useful across industry/sector, initiatives that are applicable to supporting industries as a whole (rather than industry-specific ones) would be discussed.

In order to better appreciate how policies work in Viet Nam, one has to first understand the economy’s legal structure. The Vietnamese legal structure has the National Assembly as its highest level of representation, which approves the Laws of the economy (Figure 19). As a result, Laws are placed at the highest level of the hierarchy, followed by Ordinances and Resolutions of the National Assembly Standing Committee, then Decrees promulgated by the Government, Decisions by the Prime Minister and subsequently Circulars. The policies mentioned in Decrees or Decisions are therefore subjected to the conditions of existing Laws, which may not always be consistent with the overall aims/objectives of the Decree or Decision.

Figure 19. Simplified structure of laws/regulations in Viet Nam



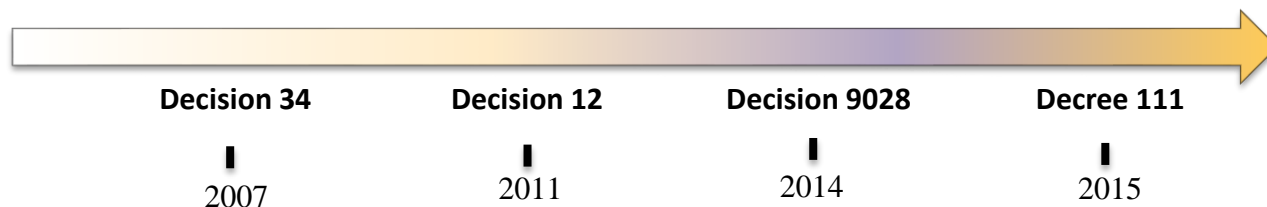
Note: There are other legislative documents such as Resolutions which are not reflected in this figure.

Source: Adapted from Law No. 80/2015/QH13

Policies specifically targeted at supporting industry development

Since 2007, the government has issued a number of regulations whose objective is to encourage the development of supporting industries. The first such regulation was Decision No. 34/2007/QĐ-BCN (‘Decision 34’) on approval of master plan of supporting industries until 2010, vision to 2020 by the Ministry of Industry and Trade (MOIT) in July 2007. It presented targets to be met by five industries (namely textiles, leather & footwear, electronics, automotive, and fabricated metal) between 2010 and 2020 and provided broad strategies for achieving these targets.

Figure 20. Timeline of supporting industry policies



Source: Authors

Subsequently, Decision No. 12/2011/QĐ-TTg (‘Decision 12’) by the Prime Minister on policies on development of a number of supporting industries was approved in 2011, and provided more details than Decision 34. In particular, Decision 12 defined the scope of supporting industries, which Decision 34 did not, and also included a sixth key industry (i.e. hi-tech industry). References to relevant decrees and specific roles for ministries and agencies were also highlighted in this later decision. For instance, the People’s Committee is required to provide updated information on regulations and programs related to supporting industries on an online portal. This Decision also made clear that MOIT would have a coordinating role over other ministries in issuing a list of prioritised supporting industry products.

In terms of incentives, Decision 12 mainly highlighted the types of assistance available for firms under existing regulations. For instance, hi-tech firms are instructed to refer to the Law on High Technology for eligible tax incentives, while SMEs are referred to Decree No. 56/2009/ND-CP on development of SMEs. The Decision also indicated that priority would be given to supporting industries in terms of funding from trade and investment promotion programs and allocation of land. Furthermore, manufacturers of supporting industry products can advertise their products on the websites of MOIT and the provincial-level Departments of Industry and Trade (DOITs).

Decision 12 was accompanied by a number of other regulations spanning 2011 and 2012 whose objectives were to further clarify some of the information including the incentives mentioned in the

Decision. For instance, Circular No. 96/2011/TT-BTC guides the financial policies indicated in Decision 12. Decision No. 1483/QD-TTg clarifies the list of products eligible for the incentives mentioned in Decision 12, while Decision No. 1556/QD-TTg targets the development of SMEs engaged in supporting industries. Decision No. 9028/QD-BCT, which approved the master plan for supporting industrial development by 2020, with a vision to 2030 then followed in 2014.

The most recent laws/regulations on supporting industry development is Decree No. 111/2015/ND-CP ('Decree 111') on development of supporting industry. It defines supporting industry as an "industry that involves manufacturing materials, accessories, components and spare parts used for assembling finished goods", with the list of prioritised products included in the annex. Similar to Decision 12, Decree 111 prioritises "new investment projects" from six key industries: a) textiles and garment industry; b) footwear-leather industry; c) electronics industry; d) automotive industry; e) mechanical fabrication sector; and f) supporting products used in high-tech industry. This list is flexible and can be updated, subject to changes in the socio-economic situation of Viet Nam. The latest addition to the Decree is Circular No. 21/2016/TT-BTC issued by the Ministry of Finance on detailed guidance of value-added tax (VAT) declarations and corporate income tax (CIT) incentives for companies producing products listed in Decree 111.

While Decree 111 falls under the main responsibility of the Ministry of Trade and Industry (MOIT), certain articles are under the purview of other agencies, as seen in Table 1.

Table 1. Agencies involved in operationalizing Decree 111 and some of their responsibilities

Agency	Examples of responsibilities
Ministry of Industry and Trade	<ul style="list-style-type: none"> Cooperate with relevant agencies to handle concerns related to the development of supporting industry Manage the list of supporting industry products Set up, manage and execute the Supporting Industry Development Program
Ministry of Finance	<ul style="list-style-type: none"> Draw up the budget for the Supporting Industry Development Program Issue detailed guidelines on tax incentives for the development of supporting products Provide information on Value Added Tax (VAT) declaration
Ministry of Planning and Investment	<ul style="list-style-type: none"> Develop incentive policies to attract foreign investment
Ministry of Environment and Natural Resources	<ul style="list-style-type: none"> Propose incentive policies on land and environment for supporting industry production projects Regulate land rent for supporting industries
Ministry of Labour, War Invalids and Social Affairs	<ul style="list-style-type: none"> Simplify the procedure for issuance of work permit for foreign workers employed in supporting industries Provide training for workers in supporting industries
State Bank of Vietnam	<ul style="list-style-type: none"> Cooperate with the Ministry of Finance and Ministry Of Trade and Industry to release guidelines on implementation of credit policies
People's Committee of Provinces	<ul style="list-style-type: none"> Formulate, amend and issue legal normative documents and policies on development of supporting industry Secure the local budget to organize the Supporting Industry Development Program Report annually to relevant Ministries and Departments on the progress of development of supporting industry

Source: Adapted from Decree No. 111/2015/ND-CP on Development of Supporting Industry

Policies for development of supporting industries can generally be categorized into two groups, namely supply-side and demand-side. As the name suggests, the former is focused on enhancing the capacity

of the firms so that they are more competitive and hopefully are able to deepen their participation in the value chain in the context of our study. The latter is focused on widening the customer base of the supporting industry firms with the hope that an expanded base would lead to improved opportunity for firms to participate in the value chain.

Analysis of assistance policies and incentives mentioned in Decree 111 into these two categories showed that they are mostly supply-side. They include funds for human resource development, R&D and technological transfers, as well as general provisions like financial assistance in the form of tax incentives and investment grants. Demand-side policies include assistance for market expansion and promotion of international cooperation. Some of these policies are elaborated below:

i. R&D and technological transfers

Firms that engage in R&D of supporting industry products are eligible for funding. They can receive sponsorship of up to 50 percent of investment costs from the Supporting Industry Development Program and other funding sources provided the project produces viable results. Land for R&D facilities will also be provided by the government. Likewise, technology transfers that benefits supporting industries are also eligible for partial funding. Additional funding of up to 75 percent will be provided to technology involving mineral processing and petrochemical products, which serve as raw materials and intermediate products for the sectors identified in the annex of the Decree.

ii. Human resource development

Firms can obtain funding for training activities from the Supporting Industry Development Program. Additionally, institutes that provide training for supporting industries can receive support from the Science and Technology Fund and Training Fund. Decree 111 also indicated that organizations such as universities, research institutes and joint venture corporations are encouraged to provide relevant training, but was not explicit if any incentives would be provided.

iii. Financial incentives

Tax incentives and import duty exemptions would be provided to supporting industry firms in line with the existing laws on taxation. Supporting industry firms are also entitled to reduced or exempted from land/water space rent. Short term loans are provided to supporting industry firms from financial institutions at an interest rate not exceeding the limit set by the State Bank. Furthermore, SMEs may take on loans of up to 70 percent of their investments, if they are able to provide collateral.

iv. Demand-side assistance policies and incentives

Decree 111 indicated that supporting industry firms would be prioritized to participate in **national** trade promotion program. Firms can also expect to receive partial funding to participate in trade fairs and exhibitions. In addition, the Decree mentioned about attracting investors and establishing relationships among organizations and individuals operating in the supporting industry. While not mentioned explicitly in the Decree, it is understood that the government conducts business matching activities which some interviewed firms have benefited from. For example, an interviewee supplying to the automotive sector indicated that whenever the government receives request from overseas for a list of potential suppliers, it would contact the firm and ask for the necessary information which would facilitate contacts between the two parties. It is understood that the government also compiles a list of

possible domestic suppliers capable of meeting the requirements of FDI firms¹⁵. Related to this is the availability of business directory in the Viet Nam Manufacturing Supporting Industry Yearbook, a publication by the Supporting Industry Enterprise Development Center (SIDECE).

Funding - The importance of Supporting Industry Development Program

Critical to the execution of many of the assistance policies and incentives mentioned above is funding. In this regard, the Decree mentioned the use of existing funds such as the Science and Technology Fund, Training Fund, and Environmental Protection Fund. The most important source of funding, however, would be those allocated to the Supporting Industry Development Program, which had just been approved in January 2017 in the form of Decision No. 68/QD-TTg¹⁶. This is because it essentially sets aside funds that are to be used only for the purpose of supporting industry development. Indeed, several of the assistance policies and incentives made direct reference to the Program. It is worthwhile to note that funding for the Program would come from both government as well as sponsorships and contributions from domestic and foreign individuals and organizations.

New organization - Supporting Industry Development Center

In addition to assistance policies and incentives, the Decree mentioned about the establishment of Supporting Industry Development Center whose responsibilities would include supporting technology transfers and training for workers in supporting industry, as well as boosting demand for supporting industry products via trade fairs and attracting foreign investment. It will also assist supporting industry firms in meeting international quality standards. Information from the Decree indicated that the Center would be established by rearranging existing units of the MOIT.

Policies to develop small and medium enterprises (SMEs)

Policies to support the development of SMEs in Viet Nam can generally be classified into two groups: i) those applicable to SMEs in supporting industries, either in the form of separate laws/regulations or as additional provisions that are only available to SMEs in laws/regulations whose target include non-SMEs such as Decree 111 discussed above; and ii) those applicable to SMEs regardless of type of industry.

Those applicable to SMEs in supporting industries

One separate regulation that ties SMEs and supporting industries is Prime Minister's Decision No. 1556/QD-TTg ('Decision 1556'), which approved the scheme "Supporting the development of medium and small enterprises engaged in ancillary industries". It was promulgated in October 2012 to increase SMEs' participation on the production network of multinational corporations (MNCs). This Decision aims to increase the number of SMEs participating in supporting industries to 2,000, and for SMEs to supply 50 percent of inputs demanded by manufacturing industries in Viet Nam by 2020.

¹⁵ See for example <http://tuoitrenews.vn/business/29142/vietnams-electronics-industry-booming-with-bright-prospects-but-changes-needed>

¹⁶ Funding breakdown is as follows: 115 billion VND to business matching activities, 231 billion VND to capacity building, 100 billion VND to human resource development, 531 billion VND to R&D promotion and 74.6 billion VND to the development and management of SI database. (Source: Presentation on *Promotion of supporting industries in Vietnam* by IPSI)

Supply-side incentives under Decision 1556 include boosting the capacity of SMEs through human resource training as well as providing technological and financial resources to support SMEs in meeting international quality standards. On the demand side, Decision 1556 aims to match SMEs that meet quality standards of MNCs. MOIT and the Ministry of Science and Technology are also in charge of developing websites and databases to provide information of supporting industries to final assemblers.

Decree 111 is a good example of regulatory tiering. It indicated that SMEs are eligible to take loans of up to 70 percent of their investment, provided they meet the required conditions. They are also exempted from, or entitled to reduced water surface and land rents, according to the Land Law. SMEs are additionally allowed to submit documents at local centres or at MOIT directly to their convenience. Other firms, in contrast, are can only make their submission to MOIT only.

Those applicable to SMEs regardless of the type of industry

The current highest level laws/regulations for developing SMEs in Viet Nam is Decree No. 56/2009/ND-CP ('Decree 56') on assistance to the development of small and medium-sized enterprises. It replaces an earlier Decree No. 90/2001/CP-ND and defines SMEs according to total capital and number of labourers which may vary between sectors. In general, firms with less than 300 employees and total capital of less than VND 100 billion (US\$ 4.4 million) can be considered as SMEs. Unlike Decree 111 on supporting industries which is under the purview of MOIT, Decree 56 falls under the purview of the Ministry of Planning and Investment (MPI). However, similar to Decree 111, it is subjected to existing regulations such as the Law on Government Organisation, Law on Enterprise and Law on Investment.

As SME development is considered a cross-cutting issue, the presence of a coordinating body would go a long way to ensure that efforts in this area are consistent and well-coordinated. In this regard, Decree 56 has stipulated the establishment of the SME Development Encouragement Council (SMEDEC) whose main responsibility is to provide advice to the Prime Minister on SME policies. The Council is chaired by the Minister of Planning and Investment and has representatives from ministries, local authorities, industry associations and experts in fields such as economics and science.

Resolution No.22/NQ-CP ('Resolution 22') was later issued to support the implementation of Decree 56. It defines more clearly the roles and responsibilities of various ministries and agencies involved in SME development such as evaluating and reviewing existing policies; proposing new policies, programs and measures, as well as mechanisms to operationalize them. Additionally, Resolution 22 specifies the timeline for ministries and agencies to execute those responsibilities. Some of the assistance policies and incentives indicated in Decree 56 and/or Resolution 22 are listed below:

i. Financial Assistance

The Capital Development Fund was launched for SMEs with a capital grant from the State budget. It aims to provide funding to programs that improves the competitiveness of SMEs. The State Bank was also tasked with strengthening the capacity of financial institutions and tailoring their products and services to the needs of SMEs. Additionally, training will be provided for SMEs to meet the requirements of credit institutions.

ii. Improving technological capacity

The Development Fund for Science and Technology will be available to support SMEs with technological capacity building. The Ministry of Science and Technology together with the People's Committee will also provide funds to support issues regarding intellectual property rights.

iii. *Business Incubator*

Nursery business space and business support will be provided to SMEs to encourage them to commercialise their business ideas and technology.

iv. *Human resource development*

Training plans to enhance the business administration capability of SMEs will be formulated. The government will also create favorable environment to facilitate the participation of various stakeholders including business associations in training activities. For instance, the government is exploring the possibility of increasing investments in vocational training, to improve the quality of technical workers. Examples of existing vocational colleges include the Long An Vocational College and the Ho Chi Minh City (HCMC) Vocational college which focus on engineering-related skills (Nham and Nguyen, 2016).

v. *Market expansion*

Minimum participation rate by SMEs will be set to facilitate their attendance in activities such as trade fairs and exhibitions. The government will also be exploring mechanisms such as the granting of concessional rates to encourage SMEs to supply products and services for public use.

Box 1. Comparison of policies to develop supporting industries and SMEs: Insights from Decrees 111 and 56

Decree 111 is aimed at development of supporting industry, while Decree 56 and the accompanying Resolution 22 are aimed at development of SMEs. One issue arising from the close links between supporting industries and SMEs is whether various assistance policies and incentives embedded in these laws/regulations are complementary or duplicative. This is particularly important for a firm that is both a supporting industry firm and an SME because complementary policies would allow it to utilize and build on both sets of incentives to enhance its capability. On the other hand, duplicative or fairly similar policies would lead to challenges in identifying and deciding which incentives to apply for, particularly if accessing incentives from one decree excludes the firm from benefitting from incentives in other decrees.

Analysis of Decrees 111 & 56 and Resolution 22 shows that a significant number of assistance policies and incentive are fairly similar (Table 2). In terms of R&D and technology transfer, for example, these laws/regulations mention the availability of funding to carry out R&D activities and technological capacity building. The same can be said about human resources development, where these laws/regulations have indicated that training activities would be supported and funded.

However, there are also assistance policies and incentives that are available only in Decree 56. For example, there are policies to increase SMEs' participation in government procurement, provision of business space and support to facilitate business incubation activities as well as provision of information pertaining to regulations to SMEs

Table 2. Presence of selected type of assistance policies and incentives in Decrees 111 & 56 and Resolution 22

Assistance policies and incentives	Decree 111	Decree 56 and Resolution 22
R&D and technology transfer	✓	✓
Human resources development	✓	✓
Financial assistance	✓	✓

Land	✓	✓
Environmental protection	✓	✓
Market expansion	✓	✓
Business incubator	✗	✓
Procurement by the public sector	✗	✓

Source: Authors' analysis of Decrees 111 and 56 as well as Resolution 22

Policies relating to the general business environment

Policies that are supportive of businesses as a whole are vital. The new Vietnamese government led by Prime Minister Nguyen Xuan Phuc recognizes this and has promulgated several resolutions whose objectives include strengthening the general business environment and steering reforms in the right direction. Resolution No. 35/NQ-CP ('Resolution 35') on supporting and developing enterprises by 2020, for instance, is aimed at fostering a conducive business environment through administrative reforms, emphasising the rule of law and building capacity of enterprises. Since their last iterations in 2005, the Law on Investment and Law on Enterprise were also recently updated.

Additionally, Viet Nam has several hundred industrial parks, where firms can benefit from free land rental, corporate income and value added tax incentives, as well as import and export duty reductions for both local and foreign investors. Other benefits from being located in an industrial park include sharing common infrastructure and minimising logistics costs, reducing the need for firms to individually invest in them. Examples of such zones in Viet Nam are the Ha Noi Southern Supporting Industrial Park and Urban Services (HANSSIP), the Saigon High-Tech Park and industrial zones in the Hai Phong and Quang Nam province.

Law on Enterprise

The Law on Enterprise regulates the establishment, organization and other related firm activities in Viet Nam. Updated articles in the Law provide clearer definitions and relax some administrative regulations. For example, the procedures to obtain the Enterprise Registration Certificate (ERC), which is required by businesses before they can operate in Viet Nam, were simplified. Previously, businesses were required to declare their "business lines", or industry that they were in. The new amendment removes this requirement, and businesses are free to operate in any industry not prohibited by law (Duane Morris Vietnam, 2014). Essentially the approach has changed from a positive list to a negative list.

Furthermore, the scope for mergers is now expanded so that enterprises of different natures are allowed to merge, when previously only enterprises of the same form of investments could merge. As an example, prior to 2014, only Limited Liability Companies (LLCs) could merge with other LLCs, and Joint Stock Companies (JSCs) could merge with other JSCs. An LLC would need to be converted to a JSC before merging with a JSC, and vice versa. Under the updated law, JSCs can now merge with LLCs without the need to be converted.

Law on Investment

The Law on Investment, as the name suggests, regulates investment activities in Viet Nam. It specifies the investment requirements and the types of incentives available for different investments among others. The updated Law on Investment clarified existing definitions, as well as relaxed some

requirements (Indochine Counsel, 2015; Frasers Law Company, 2015). Firstly, it differentiates between a “foreign investor” and a “foreign invested economic organisation” (FIEO), and also provides exact requirements to be deemed an FIEO. Previously, the term “foreign owned enterprise” was used and interpreted differently by different authorities. Licensing requirements for foreign investment projects are also relaxed. Prior to 2014, foreign firms required an investment certificate (IC), which was time consuming to obtain, and can take up to several months. The updated law has replaced the IC with an investment registration certificate (IRC). This new certificate can be obtained within 15 days, or expedited to 5 working days in the case of strategic projects.

Laws on Taxes

Taxes in Viet Nam are all imposed at a national level, and there are no provincial taxes (PricewaterhouseCoopers, 2016). The current corporate income tax (CIT) rate was reduced from 22 percent in 2014 to 20 percent in 2016, which encourages foreign investment into the economy, including supporting industries. Notably, there have been recent amendments to the laws to include mentions of supporting (or ancillary) industries. The Law amendment to Tax Law No. 71/2014/QH1371 and the Elaboration of the Law on Amendments to Tax Laws No. 12/2015/ND-CP also defined and clarified additional CIT incentives for supporting (or ancillary products) in the six key industries. Additionally, Circular No. 21/2016/TT-BTC to guide value added tax and corporate tax under Decree 111 was also released in February 2016. It highlighted CIT incentives and value-added tax (VAT) procedures for supporting industries that fall under other laws such as No. 71/2014/QH1371.

Parallel activities

The government is not the only entity providing assistance to facilitate firms’ participation as supporting industry. Interviewees shared many parallel activities that their organizations are undertaking. For example, besides its main role of providing policy recommendations to government on supporting industry development, one organization is involved in provision of training as well as development of supporting industry database on an ad-hoc basis. One organization shared that it has partnered with other organizations to provide training to its member firms.

Another organization mentioned about the wide range of activities that are in place, including: a) working with United Nations Industrial Development Organization (UNIDO) under the Subcontracting and Partnership Exchange (SPX) program¹⁷; cooperation with different institutes to carry out research on supporting industries; c) hosting of volunteers whose objective is to improve the technology know-how and quality of products manufactured by supporting industry firms; d) organization of sector-specific workshops and training by practitioners; and e) carrying out training needs assessment of firms in various sectors via survey.

Yet another organization organizes annual reverse fairs/exhibitions where approximately 50 FDI firms and 50 local firms display the products they would like to buy and sell respectively¹⁸. These business matching activities minimize the search cost by both parties. The same organization also prepares detailed catalogues of local firms with the capability to provide products to FDI firms. Table 3 gives an example of information available in the catalogues. The process of preparing each catalogue, which is updated regularly to ensure accuracy of information, takes up to 5 months and involves surveys, site visits, and interviews.

¹⁷ More details about the program can be accessed at: <https://www.unido.org/spx.html>

¹⁸ The term ‘reverse’ is used to refer to firms displaying products they would like to buy domestically, as opposed to displaying products they would like to sell.

Table 3. Examples of information available in the catalogues prepared by an organization

Company name	Contact details
Company type	Quality management certificates
Business type (manufacturing, trading, etc.)	Products and accompanying activities offered such as plating, heat treatment, forging, casting, etc.
Employees	
Turnover	
Main customer	Picture of products
Origin of technology	Machines available

Source: Authors' adaptation from catalogues provided by the organization

4. ANALYSIS OF VIET NAM'S EFFORTS TO DEVELOP ITS SUPPORTING INDUSTRY

Chapter 3 has provided an overview of policies for development of supporting industries in Viet Nam. This chapter aims to analyze the economy's efforts across various areas such as the definition of supporting industry, the formulation of relevant policies and the implementation of these policies. The purpose is to identify good practices and areas for improvements, which could serve as learning points for Viet Nam and other APEC economies as they strive to strengthen their supporting industries. It is worthwhile to note that these areas are not exhaustive and is but one attempt to group the rich and diverse information that have been obtained from desk-based research and interviews with relevant stakeholders.

Definition of supporting industry

Decree No. 111/2015/ND-CP ('Decree 111') provides one clear definition of supporting industry in Viet Nam, that is, industries which are involved in manufacturing materials, accessories, components and spare parts used for assembling finished goods. The Decree also has an annex listing down the various supporting products eligible for assistance policies and incentives. Such clarity in defining the scope of supporting industry minimizes potential disagreement between parties and is important in ensuring that policies can be more targeted given the limited resources. At the same time, Articles 3 and 14 of the Decree indicates that the list can be updated periodically, hence ensuring that it is responsive to changes in the economic landscape.

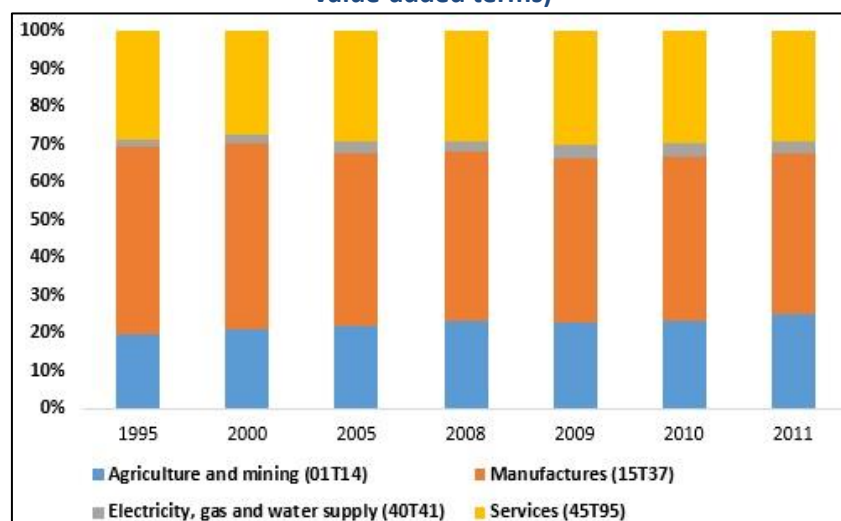
While acknowledging the benefits of clarity, some interviewees questioned the need for such a list, considering the challenge of predicting changes in trends and the fact that these trends evolve rapidly. This is especially the case for industries such as garment and footwear which follow fashion trends closely. Microfibers, which have been gaining in popularity as materials for sports shoes, are an example of newer supporting products not mentioned in the list and therefore not eligible initially for assistance policies and incentives indicated in the Decree. Although Articles 3 and 14 allow for the list to be updated, interviewees shared that the process may take some time and it is possible that firms would not be able to benefit from first-mover advantage. Certainly, it is also possible that fashion trends would have moved on by the time the list is updated.

One area that surfaced regularly is the role of services as supporting industry. There are many pieces of literature linking services and manufacturing (for example, see Miroudot et al. 2013, OECD 2013 and Kommerskollegium 2010). Indeed, measuring Viet Nam's exports of manufactured products in terms of value-added showed that the share of services in these exports has been hovering around the 30 percent range from 1995 to 2011, the latest available year from OECD Trade in Value Added (TiVA) database (Figure 21)¹⁹. Yet, as the above definition has shown, services providers are not considered as part of supporting industry. Interviewees mentioned that the general perceptions of services in Viet Nam is still from the traditional trade angle. Few understand the concept that services can be embodied in the value of goods when measured in value-added terms and hence, of the need to enhance services competitiveness for goods to be competitive as well.

¹⁹ Agriculture and mining is composed of agriculture, hunting, forestry and fishing (01T05); and mining and quarrying (10T14). Manufactures is composed of food products, beverages and tobacco (15T16); textiles, textile products, leather and footwear (17T19); wood, paper, paper products, printing and publishing (20T22); chemicals and non-metallic mineral products (23T26); basic metals and fabricated metal products (27T28); machinery and equipment, nec (29); electrical and optical equipment (30T33); transport equipment (34T35); manufacturing nec; recycling (36T37). Services is composed of construction (45); wholesale and retail trade; hotels and restaurants (50T55); transport and storage, post and telecommunication (60T64); financial intermediation (65T67); real estate, renting and business activities (70T74); and community, social and personal services (75T95).

Besides showing the important contribution of services, Figure 21 also shows to a certain extent the linkage between industries/sectors and serves to validate the question from interviewees on the necessity for the list mentioned above, which is both sector- and product-specific.

Figure 21. Share of Viet Nam’s export of total manufactures contributed by various sectors (in value-added terms)



Source: APEC PSU computations from OECD TiVA database. Accessed 12 December 2016

Policies and mechanisms for developing them

As shared in chapter 3, analysis of Decree 111 points to the presence of comprehensive range of assistance policies and incentives to develop supporting industry. While the general perception among interviewees on the policies in the Decree is positive, there is room for improvement. One such adjustment would be to clarify the exact nature of some of the assistance policies, types of activities covered and mechanisms to access them. An example would be Article 6 on human resource development – it indicated that employees involved in the manufacture of listed supporting products would be funded for training but does not elaborate on the nature of funding (to cover course fees, overseas travel, etc.), the kind of training covered (general, sector-specific, etc.), nor the mechanisms to apply for funding. Recognizing this issue, the government has further released documents to clarify them. For example, Circular No. 21/2016/TT-BTC was released to provide more detailed guidance on the tax incentives stipulated in Decree 111. Specifically on the above example, the release of Decision No. 68/QĐ-TTg in January 2017 is expected to provide clearer information. More of such documents would be helpful to firms.

Another would be to expand the assistance policies and incentives to a wider range of activities. Interviewees viewed technology adoption/absorption and R&D as critical for the development of supporting industry and noted the presence of policies to advocate such activities in the Decree. Nonetheless, interviewees found the scope of activities covered to be more focused on process improvement and less so on new materials development. They believed that the government should explore the possibility of providing support for technology management, a set of tools that would allow firms to better manage their technology such as patent utilization.

Yet another improvement is to continuously strive to enhance policies, particularly if they do not lead to the intended objectives. An interviewee noted that despite the government providing business matching services and compiling a list of possible domestic suppliers capable of meeting requirements of FDI firms, a significant number of domestic firms has not been able to benefit from them. As an

anecdotal example, it was indicated that these firms could export their parts abroad but could not supply to FDI firms in Viet Nam.

Interviewees also referred to the need for policies to take into consideration sectoral nuances and hence be tailored accordingly. It was shared that some training specific to electronics industry are not eligible for assistance and depending on the level of staff hired (such as technicians, executives and engineers), firm has to provide between 1 to 6 months of training at its own expense to bring staff to the required competency level.

Related to the above is question on how policies indicated in the Decree have been developed. A government agency brought up several mechanisms. One channel was through industry consultations via associations and pointed to the value-added tax credit as an example of incentives identified from this channel. The government also studied and adopted policies from other economies such as Japan and Korea. In addition, the drafting board of the Decree included representatives from research institutes who were able to provide recommendations by virtue of their position. Besides giving recommendations based on their own research, these research institutes organized workshops and seminars while the Decree was still in the drafting stage, providing an additional channel through which inputs from other stakeholders including industries can be collected. Interviewees viewed these mechanisms, particularly industry consultations positively but were of the opinions that the government could have incorporated more recommendations from the industry.

Awareness of policies and parallel activities

Interviewees mentioned various channels used to raise firms' awareness on the existence of policies on supporting industries. One would be via the Department of Industry and Trade (DOIT), the local-level equivalent of Ministry of Industry and Trade (MOIT) which are usually located in areas with significant presence of firms. MOIT also conducted workshops and seminars, either individually or in collaboration with industry associations, to share about available assistance policies and incentives. In addition, the Ministry consolidates all policies including those beyond its purview in a single website (<http://support.gov.vn/news/nhomvanban.aspx>) to facilitate awareness²⁰. Besides workshops and seminars, industry associations usually share information on policies via their mailing list too.

On one hand, these channels have been successful from the number of interviewees who are aware of Decree 111 – only one interviewee indicated that he/she had never heard about the Decree. However on the other hand, the interviewees may not be representative of the situation in the industry as a whole. After all, the number of applications by firms to be certified and hence be eligible for incentives remains low even after one year, indicating that awareness of the Decree among firms may be quite low.

Knowing the existence of the Decree is one part of the equation. It is also important to understand its contents such as the available assistance policies and incentives and the process to access them. Views among interviewees were mixed. Some interviewees shared that many firms have to engage the costly legal services to understand the contents of the Decree as information provided in the workshops are too general. However, others were of the opinion that interested firms should not encounter significant challenges in understanding the contents.

As indicated in the previous chapter, organizations other than the government undertake many activities to facilitate firms' participation as supporting industry. Despite the extensive number of activities, these organizations appear to have done so in a silo approach and in some cases, on an ad-hoc basis. As a result, the benefits of such activities accrue to only a small number of participants. It would be good if there is a sharing of experiences among organizations so that they can learn from one another. One possible reason for the ad-hoc nature of these activities is funding availability. If organizations have no access to funding, then it is highly likely that successful activities would not be able to continue. This

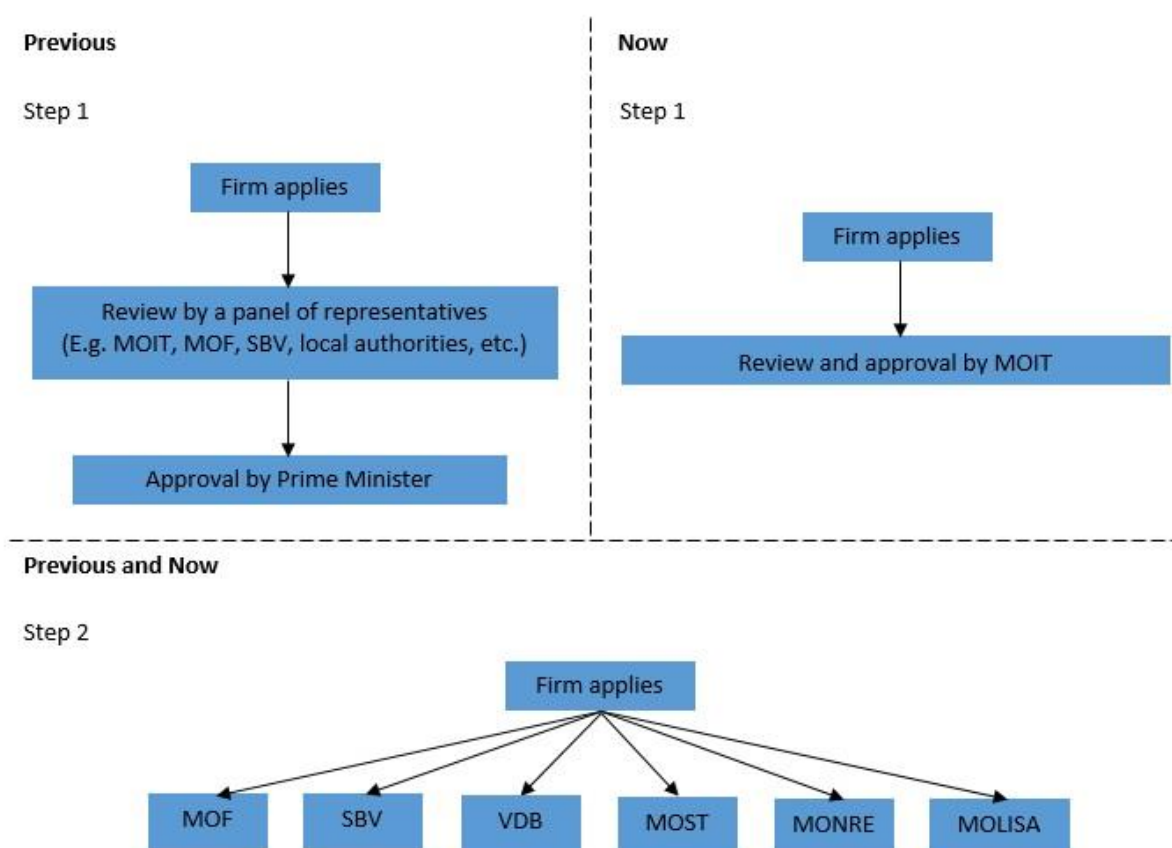
²⁰ There were 70 legal documents when the site was accessed in January 2017.

is unfortunate because many of these organizations are well aware of the needs of industries, as can be seen from the activities undertaken. While the government provides funding to some of these organizations, perhaps more can be done to ensure the continuity of successful activities and raise the awareness of their existence among potential beneficiaries.

Access to incentives and feedback mechanisms

According to interviewees, there is a 2-step process that a firm needs to undertake in order to access the assistance policies and incentives in the Decree 111: 1) apply for certification; and 2) upon certification, apply to individual agencies that administer the respective incentives. On step 1, interviewees shared that there has been simplification of procedures for firms to be certified as ‘supporting industry’. Previously, when a firm applied, its application had to be reviewed by a panel of representatives from different government agencies including MOIT, Ministry of Finance (MOF), State Bank of Vietnam (SBV) and local authorities where the firm is based before it was submitted to the Prime Minister for approval. Now, review and certification are done solely by MOIT (Figure 22).

Figure 22. Application process to access incentives indicated in Decree No. 111/2015/ND-CP



Note: MOIT = Ministry of Industry and Trade; MOF = Ministry of Finance; SBV = State Bank of Vietnam; VDB = Vietnam Development Bank; MOST = Ministry of Science and Technology; MONRE = Ministry of Environment and Natural Resources; MOLISA = Ministry of Labour, War Invalids and Social Affairs.

Source: Authors’ understanding based on interviews and Decree No. 111/2015/ND-CP

While the simplification of step 1 is a move in the right direction, interviewees felt that more could be done and called on MOIT to further clarify the definition of ‘new investment’ in Article 11 of the Decree despite having issued Circular No. 55/2015/TT-BCT. This is because some firms were informed that their planned activity could not be considered as ‘new investment’. Interviewees gave an example of a white goods manufacturer who wanted to invest in the manufacturing of certain new parts which would entail the installation of new production line but was told that it would not be treated as ‘new investment’

and hence not eligible for incentives. An interviewee shared another example whereby one of its suppliers intended to invest in the manufacturing of nuts and bolts for use in the automotive industry but was told that these parts were not 'automotive enough' and therefore not eligible for incentives.

Interviewees found step 2 to be burdensome because besides having to apply to individual agencies, they found the application process to be at the discretion of each agency and in some cases, the exact process is uncertain. Part of this lack of information can be attributed to the fact that funding for certain incentives is dependent on the Supporting Industry Development Program mentioned in Article 10 of Decree 111, which had just been approved by the Prime Minister in January 2017.

There is also no guarantee that firms would be able to access some incentives even after being certified. A certified interviewee shared that it has not been able to access any incentives so far and its certificate has only been useful to extend land use rights. With many reasons discouraging application, there nonetheless have been attempts by firms to obtain the certification. According to an interviewee, reasons to apply include showing clients that it obtains certification from the government and hope that they can benefit from the incentives when the Decree is upgraded into Law. The latter will be discussed in later section

All interviewees indicated that they are generally able to provide their views and report issues encountered to the government. The channels vary from direct contact (both official and personal) to provision of feedback via their industry associations. However, there are differences in views on whether their feedback lead to concrete actions by the government as well as the time it takes for the government to do so. One interviewee shared that it had provided feedback many times but nothing was done so far. Other interviewees indicated that their feedback usually lead to concrete actions but it may take the government some time to do so. Another interviewee shared that it makes annual presentation to the government to share some of its findings. While it usually leads to the government indicating that it would take actions, some end up not being followed up.

Policies and SMEs

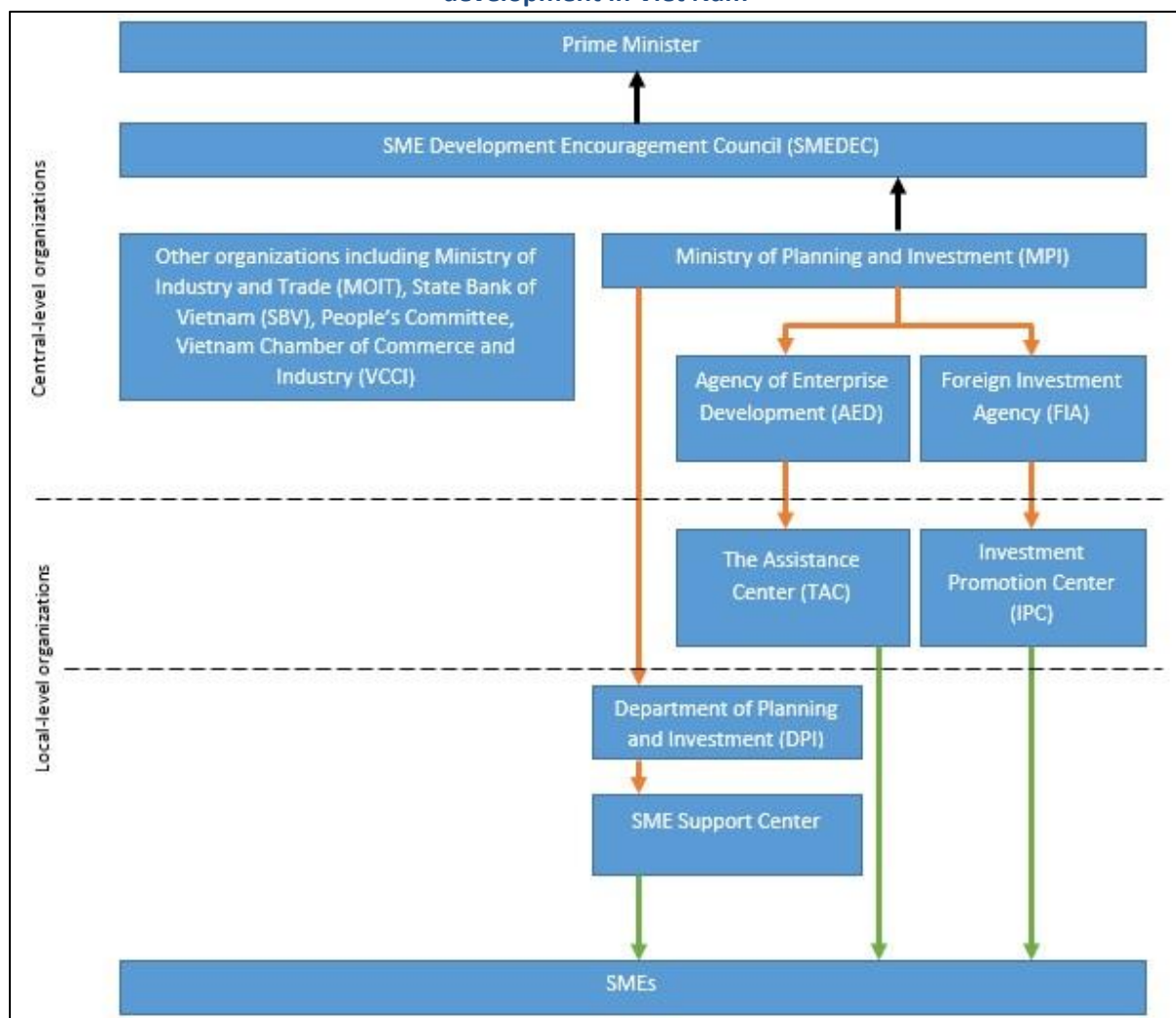
A look at the policies to support the development of SMEs in Chapter 3 shows strong commitment by the government to assist SMEs operating in Viet Nam. However, interviewees shared some areas which can be further improved. One pertains to availability of resources to implement some of the assistance policies and incentives indicated in Decree 56. Specifically for Article 7 on financial assistance, the government had established the SME Development Fund which SMEs can tap into, but it is understood that there were other assistance policies and incentives whose funding availability is still not clear.

Secondly, there are various local-level organizations which SMEs can interact with because different centers to support SMEs have been set up through several Decrees and Decisions (CIEM, 2016). Specifically on agencies under MPI, The Assistance Centers (TACs) were set up in each of the three municipalities of Ha Noi, Da Nang and Ho Chi Minh City to provide various services such as technical advice, training and information sharing (Figure 23). Then, there is the Investment Promotion Center (IPC) in some provinces whose responsibilities include provision of advice and information. It is understood that there are also SME support center in some provinces and municipality which operates under the jurisdiction of Department of Planning and Investment (DPI), the local-level equivalent of MPI. While their exact responsibilities are at the discretion of local authority and hence may differ, they generally provide information and technical support to SMEs. The presence of multiple agencies at local level providing fairly similar services brings to the fore questions on whether there is value in consolidating them so that SMEs would only need to visit one to obtain all information. Even if there are valid reasons for multiple agencies to continue, they could improve on their coordination (perhaps in the form of better understanding of their different roles) so that SMEs can be served more efficiently.

Third pertains to the coordinating role of SME Development Encouragement Council (SMEDEC). Article 16 of Decree 56 mentioned about the establishment of this Council which is chaired by the

Minister of Planning and Investment and whose members comprised of representatives from ministries, local authorities, industry associations and experts in fields such as economics and science. Its main responsibility is to advise the Prime Minister in the area of SME development. Interviewees (from MPI/AED) mentioned that in theory, the Council should lead to better coordination of efforts in this area. However, its meeting frequency and the level of representatives assigned to attend the meeting made it challenging for the Council to exercise its coordinating role.

Figure 23. Government agencies under Ministry of Planning and Investment (MPI) involved in SME development in Viet Nam



Note: By virtue of their membership in SMEDEC, there are other ministries and organizations involved in SME development. Agencies under them are not shown in this figure. Black arrow = functional flow; orange arrow = administrative flow; green arrow = services flow to SMEs.

Source: Adapted from Central Institute for Economic Management (CIEM) (2016)

Relationships between laws/regulations

Chapter 3 has clearly indicated the presence of several laws/regulations with implications on supporting industry. Of particular interest would be the relationships between them. Analysis and interviews highlight two general observations. On one hand, there are efforts to ensure consistency of laws/regulations. For instance, Decree 111 refers applicants to Law No. 67/2014/QH13 ('Law 67') on investment and Law on taxation on the types and level of investment incentives that they would be eligible for, subject to meeting the requirements stipulated in the Laws. The same Decree also refers applicants to the existing Land Law to obtain clarity on the incentives that they can access.

On the other hand, interviewees acknowledged that there are laws/regulations offering fairly similar assistance policies and incentives. In some cases, accessing incentive indicated in one law/regulation would make firm ineligible to access similar incentive indicated in another law/regulation. In others, it is possible for firm to access similar incentives mentioned in different laws/regulations. Firms are, therefore, likely to encounter two issues: 1) finding all laws/regulations providing assistance policies and incentives that they can potentially apply for; and 2) identifying which of the similar incentives to apply for, considering that they may have limited resources to pursue the finer points of legal documents. On the first issue, MOIT has established a website where all relevant laws/regulations pertaining to supporting industry including those beyond its purview can be found (<http://support.gov.vn/news/nhomvanban.aspx>). On the second issue, as shared in the previous paragraph, there are efforts to ensure consistency of laws/regulations but at the moment, the burden is on potential applicants to choose which incentives to apply for.

To a certain extent, some challenges encountered by firms in accessing assistance policies and incentives mentioned in the Decrees discussed above (such as Decrees 111 and 56) can be attributed to the structure of laws/regulations in Viet Nam. As shared in chapter 3, Laws are placed at the highest level of the hierarchy, followed by Ordinances and Resolutions of the National Assembly Standing Committee, then Decrees promulgated by the Government, Decisions by the Prime Minister and subsequently Circulars. The government's hands are, therefore, tied by laws/regulations of higher hierarchy in implementing policies. One example given by an interviewee is that while Decree 111 mentioned about the availability of corporate tax incentives, Law 67 on investment may stipulate conditions which firms have to meet in order to be eligible. In other words, even if a firm is certified as 'supporting industry' by MOIT and could apply to access the incentives indicated in the Decree, the Law may have some conditions which the firm does not meet and hence not eligible for incentives.

A look at the contents of Law 67 validates the above example. Chapters III and IV of the Law are dedicated to providing information on the types of investment incentives available²¹, investments which are entitled to the incentives, and detailed procedures to apply for the incentives. Depending on the project, authorization decision would need to be made by the National Assembly, Prime Minister or Provincial People's Committees. For added measure, Article 4 of the Law indicates that with some exceptions, the provisions of this Law shall prevail if there is any discrepancy between the provisions of this Law and those of another law. Furthermore, the government needs to submit investment incentives other than those prescribed in this Law and other laws to the National Assembly for its decision.

Many interviewees spoke of the need to upgrade Decree 111 into a Law in order to overcome some of these challenges. While the MOIT is exploring this possibility, the government is advised to ensure coordination because MPI is also looking at upgrading Decree 56 on SME development into a Law and there are already some potential issues. For example, an article in Saigon Times (2016) indicated the head of the National Assembly Economic Committee commenting that there may be overlapping regulations between the draft law on SME development and that of other laws such as Law on Investment. In addition, the draft law did not mention coordination among government agencies.

General business environment

Viet Nam's new administration has undertaken various reforms, which are mainly aimed at improving the business environment since its inauguration. As a sign of its commitment, one of the first public meetings attended by the new Prime Minister was a dialogue with the business community (ISEAS, 2017). Interviewees mentioned that it was the first time their firm was invited to share its challenges in operating in Viet Nam, when it had to be pro-active in engaging officials previously.

²¹ It was indicated in Law No. 67/2014/QH13 that specific levels of each type of investment incentives should be in accordance with the Law on Taxation and Land Law.

Despite the strong signals sent, interviewees hoped that more would be done. Predictability and constancy of policies features in the minds of many interviewees as firms make decisions with the assumptions that policies would be in place for some time. Abrupt, unannounced changes may put firms in unenviable positions. As an example, VAT surplus from import of capital goods would previously be credited to firm after 12 months, subject to firm meeting certain requirements. Interviewees shared that the policy appears to have been changed as firm has not obtained its VAT surplus even after 12 months. This means that firm has to continue servicing its debt if it borrowed money to pay for VAT when importing the capital goods.

Domestic firms interviewed have also brought up the existence of policies which inadvertently put them in a less favorable position relative to FDI firms. For instance, domestic firms need to borrow in local currency whose interest rate is around 7-8 percent. This is not the case for FDI firms who are free to borrow in other currencies with probably lower interest rate. Another example pertains to the need for domestic firms to transact in local currency – its higher depreciation rate means that firms may potentially get less considering that there are time lags between quotation and receipt of payment. Related is the need to minimize exchange rate fluctuations as it has implications on cross-border transactions.

As with other FTAs, the Trans-Pacific Partnership (TPP) was generally viewed favorably by many interviewees because it opens up markets to products originating from Viet Nam. In addition, international agreements such as TPP give government legitimate reasons to push for reforms within the economy. With the future of TPP currently uncertain, there is a worry that reforms including those enhancing the development of supporting industry may slow down or stall. As a case in point, former Minister of Planning and Investment mentioned that a recent session of the National Assembly had decided to put aside several draft laws whose objective is to introduce more reforms at a discussion in December 2016 (ISEAS, 2017).

In addition, although Viet Nam has seen improvements in some indicators as measured by World Bank Ease of Doing Business (EoDB), its ranking remains low among APEC member economies (Table 4). Viet Nam’s overall position is at number 18 when compared to other APEC economies. Analysis of its position by different areas showed that Viet Nam is at the bottom five (relative to other APEC economies) in the following areas: 1) Starting a business; 2) Getting electricity; 3) Protecting minority investors; 4) Paying taxes; and 5) Resolving insolvency.

Table 4. Ease of Doing Business in Viet Nam (DB2017)

Area	Viet Nam’s position relative to the 21 APEC economies
Overall	18
Starting a business	17
Dealing with construction permits	7
Getting electricity	17
Registering property	14
Getting credit*	10
Protecting minority investors*	17
Paying taxes	21
Trading across borders	15
Enforcing contracts	16
Resolving insolvency	20

Note: *Ties with Papua New Guinea.

Source: Authors’ analysis from World Bank Ease of Doing Business database. Accessed 23 January 2017

Other areas where further improvements can be made include infrastructure, specifically road access and overtime limits. On the latter, interviewees shared the current limit of 200 overtime hours per year

(or 300 overtime hours per year in some cases) is insufficient. To add to the challenges, there are weekly and monthly limits on top of annual limits, hence restricting firm's ability to determine where most of the overtime hours could potentially be used. For example, it would not be possible to use a significant share of the overtime hours over a period of 2 months.

Indicators of success

It is important that the government monitors the success of its policies so as to respond accordingly. Some of the indicators mentioned by interviewees are number of applications and certifications, trade balance and percentage of local content in specific sectors. On number of applications and certifications, interviewees shared that one year after promulgation of Decree 111, MOIT had received 10 applications and of these, 6 were certified as 'supporting industry' firms, which made them eligible to apply for assistance policies and incentives indicated in the Decree. Optimists viewed this as a significant improvement over what was achieved by Decision 12, its predecessor – over 4 years, only 2 applications were received and of these, only 1 was eventually certified. However, pessimists would argue that considering the number of firms operating in Viet Nam, there are many who do not have access to assistance policies and incentives.

Trade balance and the percentage of local content in specific sectors have also been used to monitor the success of policies. While these indicators are no doubt informative, their level of aggregation and broadness mean that it is very challenging to attribute the improvement in these measures, if any, to the impact of specific policies such as Decree 111.

Interviewees shared that the Annual Enterprise Census conducted by the General Statistics Office (GSO) could possibly be another source of indicators but there is a delay of about 18 months between the conduct of the census and release of results. While this is alright for academic research, it may not be acceptable for policymakers who must act quickly.

Despite the availability of these indicators, interviewees noted that more can be done to raise awareness about supporting industry. For example, information/data on SMEs do not distinguish on whether they are referring to those participating in supporting industry or otherwise. Besides raising awareness, interviewees were of the opinion that such indicators would allow for more evidence-based policy recommendations.

Capacity of middle-level and local officials

Middle-level officials have critical roles in ensuring the success of policies because they are at the forefront of policy implementation. They act as the bridge between government and businesses which are interested to explore the assistance policies and incentives they are eligible to apply for and access. As such, it is important that they understand the intent of the policies and how businesses can benefit from them. At the same time, they should also understand the need of businesses, including the technical aspects and identify how policies can assist them. In other words, officers should be able to match policies and incentives to the need of businesses. In this regard, interviewees were of the opinion that the quality of middle-level officials could be further improved. While interviewees did not elaborate on aspects where improvements could be made, a publication from CIEM (2016) pointed that most of the services provided by officials were more towards advice on administrative procedures.

Specifically on SME development, the same publication indicated that staff working at the local level in this area have limited capacity and most have not been trained or undergone re-training. In addition, majority of staff have responsibilities other than SME development.

Table 5 summarizes the good practices and areas for improvements gleaned from analysis of Viet Nam's efforts to develop its supporting industry.

Table 5. Summary of good practices and areas for improvements pertaining to Viet Nam's efforts to develop its supporting industry

Topic/area	(+)	(-)
Definition of supporting industry	<ul style="list-style-type: none"> • Clear definition of scope • Provisions to allow list to be updated periodically 	<ul style="list-style-type: none"> • Consider rationale for having a list • Definition could be expanded to include services providers
Policies and mechanisms for developing them	<ul style="list-style-type: none"> • Comprehensive assistance policies and incentives • Different mechanisms to incorporate inputs from various stakeholders 	<ul style="list-style-type: none"> • Clarify exact nature of incentives, types of activities covered and mechanisms to access them • Expand policies and incentives to cover a wider range of activities
Awareness of policies and parallel activities	<ul style="list-style-type: none"> • Various channels used to raise firms' awareness • Organizations other than the government undertake many activities to facilitate firms' participation in supporting industries 	<ul style="list-style-type: none"> • Awareness is still low when considering the small number of firms certified as supporting industries • Many of the parallel activities have been carried out in a silo approach and in some cases, on an ad-hoc basis
Access to incentives and feedback mechanisms	<ul style="list-style-type: none"> • Procedures have been simplified • There are channels to provide views and report issues encountered to the government 	<ul style="list-style-type: none"> • No guarantee that firms would be able to access some incentives even after being certified • Variation in views on whether feedbacks lead to concrete actions and response time • One-stop shop could be set up to simplify access to incentives
Policies and SMEs	<ul style="list-style-type: none"> • Commitment to facilitate SMEs' participating as supporting industries 	<ul style="list-style-type: none"> • Non-availability of funding in some cases • Coordination among agencies and local-level organizations could be strengthened
Relationships between laws/regulations	<ul style="list-style-type: none"> • Efforts to ensure consistency • Consolidation of laws/regulations on supporting industry in a single website 	<ul style="list-style-type: none"> • Hierarchy of different laws/regulations lead to challenges in implementing policies
General business environment	<ul style="list-style-type: none"> • Strong signals sent by the new administration 	<ul style="list-style-type: none"> • Predictability and constancy of policies can be improved • Ranking of the economy remains low among APEC member economies • Several draft laws to introduce more reforms have been put aside in response to current global landscape

<p>Indicators of success</p>	<ul style="list-style-type: none"> • Increase in the number of applicants certified as supporting industry firms 	<ul style="list-style-type: none"> • Level of aggregation and broadness of indicators make it difficult to attribute improvement in these measures to the impact of specific policies • More can be done to raise awareness about supporting industry. E.g. information/data on SMEs do not distinguish on whether they are referring to those participating in supporting industry or otherwise
<p>Capacity of middle-level and local officials</p>		<ul style="list-style-type: none"> • Quality of middle-level officials could be improved as the services provided were more towards advice on administrative procedures • Staff working at the local level on SME development have limited capacity and most have not been trained or undergone re-training. Majority of staff have other responsibilities as well

Source: Authors' analysis of information obtained through desk-based research and interviews

5. CONCLUSION

Viet Nam is a rising economy at the crossroads of the manufacturing world. It has been successful in attracting FDI, an important contributor to the development of its manufacturing sector and its overall growth. With progress and changing global landscape, however, it can no longer rely on low labour cost to continue attracting FDI. Furthermore, the economy needs to bolster its industrial capability and move up the value chain if it is to sustain its growth and avoid middle income trap. One area which the economy can work on is improving the state of its supporting industry, which is relatively weaker than their counterparts in other APEC middle income economies.

Acknowledging this, the government has promulgated a number of laws/regulations which have implications on the development of its supporting industries, either directly or indirectly. Special attention is also paid to SMEs, which make up approximately 97 percent of firms in Viet Nam and are a major source of employment and contributor to its economy. Analysis of recent laws/regulations, their development as well as implementation process across various measures showed that the government has undertaken many actions that could be considered as good practices. For example, it provides one clear definition of supporting industry (through Decree 111) to minimize disagreement and ensure that policies can be targeted given the limited resources. There is also a wide range of assistance policies and incentives whose objectives are to overcome the challenges faced by supporting industry firms.

In terms of policy development process, the government employed several mechanisms including industry consultations, incorporating inputs from the academia as well as studying and adopting relevant policies from other economies. It has also simplified part of the application procedures to access the incentives indicated in the laws/regulations. In addition, it utilizes various channels to raise firms' awareness of policies such as conducting workshops and seminars, consolidating all policies in a single website and asking their local authorities/agencies to provide information to the firms directly.

However, this case study also identifies some areas of improvements. For example, given the unpredictable and rapid change in trends in certain industries the government may want to re-consider the usefulness of a list of supporting products which are eligible for incentives. An outdated list may prevent innovative firms from accessing the indicated incentives and therefore, benefiting from first-mover advantage. Also an issue to be contemplated is whether the economy should expand the definition of supporting industry to include services providers such as firms providing logistics and legal services since the two sectors (i.e. services and manufacturing) are closely linked.

Another area is the exact nature of the assistance policies and incentives indicated in the laws/regulations. While there is no doubt on their intent, there is a dearth of information on the nature of the incentives, types of activities covered by the incentives and mechanisms to access it. While there is progress on this front through the release of circulars for instance, more of such documents would be helpful to firms. Pertaining to procedures to access incentives, though the government's effort to simplify them is laudable, existing procedures can be further enhanced. A case in point is step 2 of the process to access incentives indicated in Decree 111, which requires firms to apply to individual agencies that administer the respective incentives.

Specifically on policies with implications on SMEs, there is strong commitment by the government to assist with SME development, but its efforts can be further enhanced in areas such as funding and coordination between multiple agencies involved in this endeavor. Last but not least, it is imperative that the inconsistencies between the myriad of laws/regulations that affect supporting industry are resolved. These areas of improvements, if addressed properly, could put Viet Nam in a prime position as it continues to strengthen its supporting industry.

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ANNEX

Table 6. List of Interviewees

No.	Organization	Category	Specific supporting industry (if applicable)
1	Heavy Industry Department – Ministry of Industry and Trade	Government	-
2	International Cooperation Department – Ministry of Industry and Trade	Government	-
3	Agency for Enterprise Development – Ministry of Planning and Investment	Government	-
4	Institute for Industrial Policies and Strategies (IPSI)	Research institute	-
5	Central Institute for Economic Management (CIEM)	Research Institute	-
6	Viet Nam Chamber of Commerce and Industry (VCCI)	Industry association	-
7	Viet Nam Leather, Footwear and Handbag Association (LEFASO)	Industry association	Footwear and leather
8	Viet Nam Electronic Industries Association (VEIA)	Industry association	Electronics
9	Viet Nam National Textile and Garment Group (Vinatex)	Firm	Textile and garment
10	Machines and Industrial Equipment Corporation (MIE)	Firm	Mechanical fabrication
11	Ha Noi Plastics Company	Firm	Automotive
12	Toyota Motor Viet Nam	Firm	Automotive
13	4P Company Ltd.	Firm	Electronics
14	Japan External Trade Organization (JETRO)	Non-profit	-