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Abstract: This paper discusses the changing relationship between the EU and Vietnam, and asks whether there is a shift from a "parental" to a "competitive" relationship. The focus of the paper is on the shift from aid to trade as the main interface between the EU and Vietnam. Aid relationships are often understood as hierarchical, linking a benevolent donor to a needy recipient, whereas commercial relationships are typically expected to involve a more competitive relationship. However, we argue that the bilateral relationship was never a "parental" one, even at the time when Vietnam's relation to the EU was limited to aid. The reason is largely Vietnam's historical experiences from the aid relationship with the Soviet Union, which created dependence and eventually an economic crisis when aid flows dried up in the late 1980s. Instead, there has been substantial tension between the donor community and Vietnam during most of the period since the early 1990s, when aid flows from the EU started growing. Regarding trade relations, we note that the EU's increasing use of antidumping tariffs against Vietnamese exporters during the past years could be an indication of a less friendly and more competitive attitude towards Vietnam. However, it is likely that the antidumping measures used by the EU are not primarily directed at Vietnam, but rather at China. This means that Vietnam is affected by the re-polarization of the world economy through its proximity to and links with China, but that the relation is perhaps not as bad as the increasingly frequent trade conflicts may suggest.

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1. Introduction

The relationship between the European Union and Vietnam is interesting for several reasons. Most importantly, Vietnam is a rapidly developing emerging economy that is becoming an interesting market and production location for European business, as well as a notable exporter with the European market as one of its main targets. Few developing economies have been able match the economic performance of Vietnam: China is the only country that has clearly been able to exceed the Vietnamese growth record over the past two decades. This change in Vietnam's development status – from one of the least developed countries 30 years ago to an emerging economy today – has had an inevitable effect on the relationship between the EU and Vietnam.

A quick glance at the evolution of the links between the EU and Vietnam might suggest that it is a good illustration of the repolarization discussed in this volume. In the past, the relationship was mainly centered on official development assistance (ODA), with more than a dozen EU countries and the EU commission supporting Vietnam with grants, credits, and technical assistance. Much of the support aimed to facilitate Vietnam's internationalization – infrastructure, private sector development, and trade reform (e.g. support to Vietnam's WTO accession) were important areas of collaboration. However, during the past few years, attention has turned to more contentious issues. A few of the main bilateral donors have closed (or are planning to close) their bilateral ODA programs: in the case of Sweden, the termination of the ODA program has partly been a protest against Vietnam's lack of progress in human rights and democracy. Increasing friction has been noted also in the economic area. A number of highly publicized EU antidumping cases have restricted the ability of Vietnamese firms to reach the EU market. Leather shoes, bicycles, and fluorescent lamps are examples of Vietnamese export products that have allegedly been "dumped" on the European market, according to the EU commission.

The purpose of this paper is to examine how this changing relationship between the EU and Vietnam should be understood. Is it a shift from a "parental" to a "competitive" relationship? Or will it be possible to maintain a development oriented relationship even in a more polarized world economy? Section 2 below provides a background by briefly describing Vietnam's macroeconomic development during the past two decades, Section 3 looks at the aid relationship. One of the arguments presented in the section is that the bilateral relationship was never a "parental" one, largely because of Vietnam's historical experiences from the aid relationship with the Soviet Union. Instead, there was substantial tension between the donor community and Vietnam during most of the past 20 years. Section 4 turns to the trade relationship. It begins by outlining Vietnam's trade policy environment before 2007, and continues with a discussion of how it has changed as a result of WTO membership. EU's increasing use of antidumping tariffs against Vietnamese exporters in recent years could be an indication of a less friendly and more competitive attitude towards Vietnam. However, we argue in this section that the antidumping measures used by the EU are not primarily directed at Vietnam, but rather at China. This means that Vietnam is affected by the repolarization of the world economy through its links with China, but that the relation is perhaps not as bad as the frequent trade conflicts may suggest. Section 5 concludes, stressing the fact that the repolarization of the world economy forces small countries like Vietnam to navigate in a much more complex international environment than during the past couple of decades.

2. The Macroeconomic Context

Vietnam's macroeconomic development during the past decades has been remarkably successful, with high growth rates and reasonably stable prices. Real annual GDP growth has averaged nearly 7.5 percent since 1990, with the official growth rate in 2009 reaching 5.3 percent, in spite of the global financial crisis. As a result, real per capita incomes have quadrupled over the past 20 years – nominal per capita income has grown from about $100 in 1990 to over $1,000 in 2009. After some years of high inflation following the liberalization of state-controlled prices in the mid-1980s, the inflation rate dropped to single-digit levels, and has remained below 10 percent almost every year since 1990.The main exception is a temporary inflation peak in 2008, when prices rose by 23 percent.

In the early 1990s, growth was fuelled by the opportunities opening up as decision-making was decentralized to individual state-owned enterprises and the contacts with market economies – and their multinational corporations – started growing. The domestic private sector emerged as an important actor in the late 1990s, and the number of registered private enterprises started growing rapidly after the introduction of a new enterprise law in 2000. This law was not only a sign that private enterprise had become politically acceptable, but it also simplified the complex licensing procedures that had been required to set up new private firms. As a result, the modern private sector is the most dynamic part of the Vietnamese business community today, in particular with regard to employment creation. In recent years, growth has been fuelled mainly by high investment rates – more than one-third of GDP is devoted to investment – and rapid export expansion. Vietnam's export volume has nearly quadrupled since 2000 and exports amount to about 60 percent of GDP. Table 1 summarizes the data on these achievements, together with some additional information about the structure of the Vietnamese economy.

Foreign investors have been important both for investments and export growth since the mid-1990s. The inflows of FDI grew rapidly from around 1993, and the annual investments amounted to $1.5-2.5 billion until 2007, with an increase to nearly $10 billion during the last few years. Foreign-invested enterprises now account for nearly one-fifth of GDP, nearly one-third of total investment, and more than half of total exports including crude oil (excluding crude oil, the FDI share of exports is about one-third). Yet, the state sector still holds a dominant position in the Vietnamese economy. A remarkable observation is that the state holds a larger share of GDP today than in the early 1990s. This may appear contradictory taking into account the progress of the private sector. One reason is that the GDP share of the non-state sector includes agriculture, which dominated the economy two decades ago, and where growth rates are substantially lower than in industry and services. The role and importance of the private sector is easier to distinguish in manufacturing, where an increasing share of output, employment, and exports come from private firms.

Table 1 **Macroeconomic Development in Vietnam 1990-2009**

	1990	1995	2000	2005	2008
GDP (billion $)	6	21	31	53	92*
Real GDP growth (%)	5.1	9.5	6.8	8.4	5.3*
GDP per capita ($)	98	288	402	635	1060*
Inflation rate (GDP deflator)	72.8	17.0	3.4	8.0	6.7*
Merchandise exports (billion $)	2.4	5.4	14.5	32.7	54.8*

Merchandise imports (billion $)	2.7	8.2	15.6	37.8	66.3*
Current account (% of GDP)	-4.0	-8.3	3.6	-1.5	-8.3
External debt (% of GDP)	359.6	122.6	41.1	36.2	28.9
GDP composition by economic sector (% of GDP)					
Agriculture	38.7	27.2	24.5	20.9	21.3
Industry and construction	22.7	28.8	36.7	39.5	40.0
Services	38.6	44.0	38.8	38.0	38.7
GDP composition by ownership (% of GDP)					
State	31.7	40.2	38.5	38.4	34.4
Non-state	63.0	53.5	48.2	45.6	47.0
FDI	5.3	6.3	13.3	16.0	18.7
Structure of investment by ownership (% of total investment)					
State investment	34.2	38.3	58.2	51.5	28.6
Non-state investment	33.7	29.4	19.4	32.2	40.0
FDI	32.1	32.3	22.4	16.3	31.4

* Data for 2009.
Sources: EAEP (2006); CIEM (2006); Nguyen *et al.* (2006); World Bank Databank. http://data.worldbank.org/country/vietnam.

It is not only in the economic sphere that Vietnam has recorded substantial improvements during the two decades since market oriented reforms were initiated. Vietnam's health indicators have improved substantially since the late 1980s (although many of the improvements did not commence until 1992-1993). For instance, life expectancy at birth increased from about 65 years around 1990 to about 73 years at present. The total fertility rate has declined sharply over the same period, from 3.8 to below 2. Child mortality and maternal mortality rates have diminished even faster. Many vaccine-preventable diseases have also been brought under control through broad immunization programs, and the share of deaths caused by infectious disease declined from over one-half in the mid-1980s to about one-third in 1999 (MoH, 2002). Some diseases like polio and infant tetanus have been eliminated altogether (MoH, 2002, SRV 2005).

However, in spite of the overall success, there are areas where the remaining challenges are serious. Macroeconomic stability is one example. The high GDP growth rate reflects high aggregate demand, and there is a risk that bottlenecks in the domestic economy will generate inflationary pressures. The situation in 2008, when the inflation rate rose above 20 percent, illustrates how sensitive the economy still is. A large share of the macroeconomic challenges are related to the development of the international oil price: Vietnam is a major exporter of crude oil, but also a substantial importer of refined oil products. Rapid increases in oil and gas prices might have severe effects, both directly and indirectly. Higher energy prices leave a strong direct imprint on consumer prices and contribute to the general problems related to high inflation: increasing uncertainty, higher nominal interest rates, and redistribution of wealth from current income earners to holders of real assets are all likely to reduce the growth rate of the economy. At the same time, oil contributes strongly to government revenue, and increasing oil prices tend to create budgetary resources for expansionary policy, which may also be inflationary.

The continuing dominance of the state sector is another challenge. Although the state sector controls much of the country's investment resources, there are worries that the investments are not efficient. The direct employment generated through state investment is small – the total employment in the state sector amounts to about 10 percent of the labor force and has barely increased during the past decade – and there are frequent complaints about problems at all stages in the public investment process, ranging from planning to implementation (CIEM, 2005). One of the long-term responses to these weaknesses is the *equitization* of state-owned enterprises, which is intended to establish harder budget constraints and more efficient and business-oriented management practices in the state sector. However, the annual equitization targets have systematically been missed, and there are numerous problems slowing down the process. The most important ones appear to be resistance from SOE managers, problems regarding the valuation of state assets, and legal uncertainties connected to the restructuring and equitization of the largest government conglomerates, the so-called General Corporations. To maintain high growth rates, it will be necessary to accelerate the pace of SOE reform in coming years: one consequence of Vietnam's accession to the WTO in 2007 was that it has become increasingly difficult to discriminate against other enterprise types in order to protect inefficient SOEs.

Yet another potential problem is related to the country's external balance. In spite of the high export growth rates, Vietnam's merchandise trade balance has recorded deficits of 13-15 percent of GDP during the past few years. Adding other current account transactions (services and transfers, e.g. overseas remittances and ODA), the deficit has been reduced to about 8-9 percent of GDP, as shown in Table 1. While Vietnam does not appear to have any problems in covering this deficit in the short run – the inflows of FDI and foreign credits are normally more than sufficient to cover the current account balance, and external debt is not alarmingly high – it is essential that the import surplus is used to raise the country's long term competitiveness. The concerns in this area are related to the efficiency of investment, including state investment. Much of the trade deficit is probably connected to investments in SOEs and public infrastructure, which could be expected to raise future production capacity. However, this expectation assumes that the investment resources are used for projects that yield a sufficiently high social return. For investments in state-owned industry, a key question is whether enterprises will be able to survive in the more competitive climate that can be expected as Vietnam's trade barriers are gradually reduced in the future. The fact that the capital inflows to Vietnam are presently at a high level – easily comparable to those in China on a per capita basis – does not reduce these concerns. On the contrary, the availability of large amounts of capital makes it important to invest available funds efficiently, since there are often important lock-in effects of investments. Once large amounts of funds are committed to specific projects, they create interest groups that benefit from these investments and that are likely to try to maintain *status quo* even when it would be socially beneficial to change the direction of policies. Some of the difficulties in the negotiations about Vietnam's WTO membership before 2007 were probably caused by investment decisions made in the state sector already in the mid-1990s: much investment was targeted to sectors where Vietnamese producers were competitive only thanks to protection from imports (see Kokko, 1997).

The emerging income and welfare gaps in Vietnam make up a further policy challenge. Although the overall growth performance of the economy has been laudable – and although Vietnam has managed to cut the incidence of poverty by more than half since the late 1980s – there are worries about the distribution of income and wealth. High economic growth is a strong priority for the Vietnamese leadership, for several reasons. A high economic growth rate provides some degree of legitimacy to Vietnam's one-party Communist rule: it may be argued that alternative political systems might be less efficient, consuming more resources for the political struggle between parties and interest groups and leaving less for productive investments. Even more importantly, a high growth rate is considered as a precondition for social stability. Given that initial wealth, human skills, and opportunities are not perfectly equally distributed in any society, and that economic development is a process where relative prices are in constant change, it can be argued that a certain minimum growth rate is necessary to ensure that all (or almost all) social groups benefit from economic development. Growth rates lower than this minimum might leave some groups worse off, which would cause discontent and might result in political protests and opposition against a system that is not perceived as "fair": hence the need to generate sufficiently high growth. However, it is clear that income inequality has been rising in Vietnam over the past decade (see Glewwe *et al.*, 2004). This is true both in a geographical and a social dimension – some regions are growing substantially faster than others, at the same time as some social groups fare much better than others. Geographically, growth is concentrated to Vietnam's two urban centers – Hanoi and Ho Chi Minh City. The so-called *socialization* of health and education (which actually entails moving a larger part of the financing burden from the state budget to the users of the services, i.e. the relevant social groups) is an example of a policy that may have contributed to increasing social gaps (Kokko and Tingvall, 2008). There is no doubt that some of these gaps will need to be addressed by policy makers to ensure continued smooth macroeconomic development.

3. Relations with the EU: Overseas Development Assistance

In spite of Vietnam's rapid development during the past two decades, it remains a relatively small and poor economy: the country's nominal GDP is only $92 billion, which is comparable to the purchasing power of a medium-sized European city, like Stockholm or Copenhagen. Adding the long distance between Vietnam and Europe, it is not surprising that the economic relations between the two regions have been limited until recently. Vietnam has not been an important market for European firms, and Europe's foreign direct investment in Vietnam has been small compared to that of the US and regional investors like Japan, Malaysia, Singapore, and Taiwan. Still, the political relations between the EU and Vietnam have been remarkably strong. The historical colonial links between France and Vietnam, coupled with the contacts established during the 1970s and 1980s between Vietnam and several Eastern and Central European countries (within the framework of the COMECON) and the (Northern) European political support to Vietnam during the American War, have all contributed to various kinds of interactions and contacts. A large part of these relations have been centered on ODA.

It is not only the EU that provides aid to Vietnam: in fact, Vietnam has become one of the favorite aid recipients of many multilateral and bilateral donors during the past decade. It is presently the world's third largest recipient of ODA after Iraq and Afghanistan. In many countries that receive substantial amounts of aid, there is a more or less "parental" relationship between the donors and the recipient. The implicit assumption is often that the donor has superior knowledge of policy making and macroeconomic management, and that the recipient should follow the policy advice provided by donors. Often, aid disbursements have even been conditional on specific reforms – the aid programs have essentially been "owned" by the donor community. However, this has not been the case in Vietnam.

Aside from its good economic performance – donors are pleased to see progress in economic development and poverty reduction – Vietnam is popular because it is perceived as a "good" aid recipient. In fact, Vietnam is sometimes identified as the "best practice" example of ODA management and recipient ownership of the development agenda (Forsberg, 2007; GRIPS, 2002;

UNDP, 1996). During the past few years, most donors have accepted the priorities and objectives defined by the Vietnamese government and aligned their activities with the official development strategy (Jacquemin and Bainbridge, 2005).

Vietnam's strong ownership and the present framework for ODA management are largely based on experiences from the 1970s and 1980s, when the country became heavily dependent on the Soviet Union. Since that time, Vietnam has been careful to avoid similar dependency in the relations with other foreign countries – a prime rule for engagement with foreign countries has been to preserve the autonomy of the nation.

The economic sanctions that were introduced by the West and many Asian countries after the Vietnamese decision to send troops to Cambodia in 1978 led to the withdrawal of most of the ODA that had started to flow into the country after the end of the Vietnam War in 1975. Sweden, Finland, and the UNDP were the only Western donors that continued supporting Vietnam, albeit at a small scale. Instead, Vietnam was forced to move closer to the Soviet Union and the European communist bloc for external assistance and trade relations. Throughout the 1980s, when the weaknesses in the centrally planned economy resulted in stagnation and macroeconomic instabilty, the Vietnamese economy survived primarily thanks to Soviet aid. According to Pike (1987), at its peak in the mid-1980s, Soviet aid made up about 10 percent of GDP and covered more than 40 percent of the government budget and 75 percent of total public investment. At the same time, the share of trade with the Soviet Union reached about 70 percent of Vietnam's total foreign trade. The support from Sweden, Finland, and the UNDP is estimated to have reached only about one-tenth of what was provided by the Soviet bloc.

The reliance on aid from the Soviet bloc forced Vietnam to implement a political agenda – both domestically and internationally – that was largely outlined by the Soviet Union. However, the substantial aid flows did not contribute much to Vietnam's ability to create a sustainable foundation for economic development. The disintegration of the Soviet Union at the end of the 1980s, which ended the aid inflows from the Communist bloc, therefore had a severe impact on the country. The economy stagnated at the same time as inflation accelerated. One particularly troublesome consequence was a fall in food production – although few people suffered from starvation, it is clear that a majority of the population was below the food poverty line. These circumstances led up to the introduction of the market oriented reform package that became know as *Doi Moi*. Together with the withdrawal of Vietnamese troops from Cambodia in 1989, the reforms contributed to the return of aid from Western countries a few years later. The government quickly facilitated the normalization of relationships with major donors and introduced aid as an important external resource for the on-going reform process (MPI, 2004).

Yet, the relations with donors were managed very cautiously. The strategy aimed to avoid too much dependency on one power, and the Vietnamese government also hesitated to deal with donors as a unified bloc. This caution remained for a long time after the *Doi Moi* reforms to avoid the risk that foreign assistance could be used to influence Vietnam's domestic affairs. The principles laid down by the Politburo state that the relations with external actors should contribute to "self-determined integration, bringing into play the nation's internal forces and taking most advantage of integration in order to strengthen effectiveness of international cooperation, ensuring independence and ownership as well as national interests" (Politburo Resolution No.07-NQ/TW 2001:3, Central Party Committee). Consequently, the government has generally resisted development projects where a donor's policies and aid disbursements are tied to strong political or economic conditions. Strong autonomy and ownership of ODA policies has been maintained to avoid aid dependency.

Another explanation for the strong sense of recipient ownership is that many donors represented in Vietnam today arrived after the market-oriented reforms were initiated by the Vietnamese leadership. This is important for Vietnam's relations to donors, as it makes it clear that foreign aid was not the initial driver of the economic advances that have taken place over the past two decades. Moreover, the reforms resulted in rapid economic development that enabled Vietnam to avoid taking on substantial amounts of foreign debt. Taken together, these factors have strengthened Vietnam's bargaining position, making Vietnam different from many other aid recipients and their relations to donors: the Vietnamese government controls its agenda to a higher degree. Donor support remains strong today, with annual aid flows increasing from a few hundred million dollars in 1990 to nearly $3 billion in recent years. Japan, ADB, and the World Bank have accounted for 70-75 percent of total aid inflows during the past decade, with the EU contributing most of the remainder.

Although the purely financial aspects of foreign aid have been important for Vietnam, it is important to note that donor community plays a more important role than just financing Vietnamese development. Over time, donors have become important policy dialogue partners and have influenced Vietnamese policy making in various ways (UNDP, 2005). This is also the area where the EU has made the biggest impact on Vietnam. As we will argue below, the EU has probably been more important as a catalyst for institutional change than what is reflected by its financial contributions to Vietnamese development.

Institutional design: ODA in a centrally planned economy

Given the lessons from the relationship with the Soviet Union, the Vietnamese government has always had a strong ambition to control its domestic politics. In the area of development cooperation, central planning has until recently been the fundamental tool of the government to manage and regulate socio-economic policy and development. The institutional setup put the Ministry of Planning and Investment (MPI) at the centre of the country's overall national development planning. In this central role, MPI drafted and formulated the overall national development strategies and short-term plans, and was responsible for the management of public investment and resource allocation. MPI was rightly considered a super-ministry - a "conductor of the whole development concert in which the musical players in the orchestra are inputs from different ministries", as noted by MPI officials. The main task of MPI was to manage the government's development priorities and to balance stakeholder interests between sectoral and regional concerns, as well as between national and international actors.

The integration of ODA into the national development plans was part of this institutional set-up, making MPI the central actor for aid integration and coordination. This suited the central planning system, but was also a wish from donors, especially multilateral donors such as UNDP and the WB. Hence, MPI held the leading role among the ODA coordinating agencies, which also included the State Bank of Vietnam, the Ministry of Foreign Affairs, the Ministry of Finance, and the Office of Government. Within MPI the main responsibility was given to the Foreign Economic Relations Department (FERD). MPI/FERD coordinated and managed ODA resources at the national level, including negotiating, supervising and coordinating the allocation of most ODA programs, in particular large-scale and capital-intensive loan projects. Vietnam's national development plans were the instruments used to integrate donors' aid programs with the government's preferences. Based on the socio-economic development plan and the 5-Year Public Investment Programs (PIP) prepared by MPI, FERD prepared a priority list of national projects calling for ODA investment during the current five-year planning period. This priority list was in fact a "menu" for donors to select projects for their development cooperation. In this setting, it was clear that various donor projects were expected to conform to the framework given by Vietnam's development plans.

What characterized the system, at least on paper, was that MPI was responsible for overall development as well as aid integration and donor coordination, which helped the government exercise strong ownership over the overall development agenda. MPI's most important task was to make sure that ODA matched Vietnam's development priorities and to oversee when development plans required aid interaction. The resulting structure for ODA management had three main characteristics:

(i) The state regulated not only domestic development planning, but also the allocation of aid and the relations with donors. The central position of MPI was instrumental in creating strong ownership. If donor and aid management had been outside the body responsible for national economic planning, it would undoubtedly have been more difficult to align aid flows with Vietnamese development priorities. In addition, donors were given a window for policy dialogues, making it possible for donors to have some impact on national development planning.

(ii) MPI was mainly responsible for the coordination and management of loan aid, which has constituted 60-70 percent of total ODA in financial terms from 1996 (UNDP, 2005). This arguably gave more influence to donors like the WB and Japan, who accounted for most of the loan aid to Vietnam. Smaller bilateral donors, who provided more technical assistance and grant aid projects, were in a weaker position to influence Vietnamese development policy. They participated in the top level dialogue, e.g. as as contributors to multilateral credit packages, but most of their direct contacts were with provincial and sectoral authorities. Heads of line ministries and provincial people committees were only entitled to approve smaller technical projects.

(iii) The incentives and capacity of line ministries and provincial agencies were formally constrained by the centralization of power to the MPI. Overall, the government exercised a system in which it planned, steered and controlled local governments through the provision of public services and infrastructure, including those investments that were financed by ODA. Dapice (2002) argues that under central planning, aid became a strongly politicized process, where provinces had to turn to Hanoi in order to convince MPI that their development projects were of higher priority than others, and that they should be included in the priority lists presented to donors.

Did ODA undermine central planning?

However, it was not easy to maintain central control of ODA in an economy undergoing rapid structural change, and the role of MPI has slowly begun to change in recent years. The centralization of power to the centre did not only constrain the dynamism of provincial development and the economic autonomy and accountability of local authorities, but it also created other problems. For example, the dominance of MPI created a strong bias towards physical investment and economic growth, with much less attention to social issues and "pro-poor" expenditures than what most donors desired. Among the donors, it was mainly the World Bank, the Asian Development Bank, and Japan that collaborated directly with MPI. These donors were the largest creditors to Vietnam, and they also had a strong focus on infrastructure and other investments that were relatively easy to adapt to the Vietnamese central plan. The European Union's aid portfolio was divided between the EU Commission and a dozen bilateral donor agencies, each of them with their own specific development agenda. Some credits for infrastructure development were included in the EU portfolio, but the emphasis was on "softer" issues, and there was a preference for technical assistance and institutional support rather than credits. These projects were more difficult to administer as part of the central planning system. Some decentralization was therefore allowed, so that donors and various domestic actors (mainly related to the state – provincial authorities and line ministries) could agree about smaller aid projects without the need for MPI approval.

The emphasis on growth and infrastructure was very obvious in the investment programs undertaken during the 1990s. "Modernization and industrialization" were the main objectives of the 5- and 10-year plans, and a large share of available resources was invested to create the infrastructure needed for economic growth. During the first half of the 1990s, the emphasis was on water and sanitation, during the second half of the century focus shifted to energy, and after 2000, priority was given to transportation. Social issues had lower priority, and were handled through various national programs that targeted the poor mountainous areas in the northern and central parts of the country. Yet, the bulk of resources, including the ODA funds, were deployed in regions that were already relatively wealthy, since it was expected that the growth effects would be larger there. One result, criticized by many donors, was that the regional income gaps started growing.

During the past decade, two processes have contributed to change the form and content of Vietnamese central planning. One is related to the increasing bargaining power of provincial authorities regarding the use of ODA. In the same way that European regions discovered that contacts with Brussels could strengthen their bargaining positions in negotiations with national authorities, Vietnamese provinces recognized that cooperation with EU (and other) donors could strengthen their bargaining power with respect to the MPI and Hanoi. Instead of waiting for MPI to add their favorite project to the list of prioritized ODA projects, provinces could first elicit funding (or at least commitments) from donors, and then turn to MPI to get the projects formally approved in the central plan. These practices turned out to complicate central planning, since many ODA projects require counterpart funding from the national budget: ODA could no longer be seen as a resource that was generated by the center, and then distributed across the country according to the priorities in the central plan. Instead, it was necessary to get advance information about what donors and provincial authorities were discussing and to assess the possible consequences of these negotiations for public expenditure before the central plan could be finalized.

It can be argued that the EU played a particularly important role in this process. Unlike Japan, ADB, and the World Bank, which operate large centralized programs where concessional credits are the main form of aid, the EU carries out many small projects in different sectors and provinces, relying much more on technical assistance and support to institution building. In recent years, the aggregate EU portfolio has included 15 bilateral donors and the EU commission, each with a variety of projects with different objectives and targets. The impact of each individual aid project has probably been small, and it is impossible to assess what their aggregate impact on Vietnamese development has been. However, at the macro level, it is clear that the aid relationship with the EU has had a very important impact on Vietnam. The fragmentation of EU aid has actually contributed to transforming Vietnamese central planning towards a more consultative process where provincial authorities and other interest groups have been strengthened at the expense of MPI. If the EU had acted in a more coordinated manner, pooling its resources into fewer but larger projects, it is likely that MPI would have taken a more direct role in the implementation of these projects. In that case, European ODA would instead have strengthened MPI's (and the central government's) ability to uphold central planning.

The other process is related to the increasing emphasis on poverty alleviation among donors. Since the late 1990s, the donor community has shifted from demands for structural adjustment to calls for poverty reduction, with particular emphasis on health care, education, and social sectors. The aggregate Vietnamese response to the tendency towards decentralization described above and the stress on poverty reduction has been the introduction of a special planning document that summarizes the new strategies in this field – the Comprehensive Poverty Reduction and Growth Strategy (CPRGS). This document can be said to have three roles. Firstly, it presents a summary of Vietnam's overall development strategy to the donor community. A large part of ODA is made up of credits and budget support, which basically contribute to all expenditure categories in the Vietnamese government budget: budget support is fungible by nature, and it is therefore impossible to identify exactly which expenditure items it finances. Therefore, donors need a comprehensive summary of all areas that are influenced by ODA. Secondly, CPRGS functions as a more concrete and detailed plan for domestic development than the relatively abstract 5- and 10-year plans. This provides incentives for local development initiatives, since it improves the ability of provincial and local authorities to develop plans that are consistent with the policies of the central government. Thirdly, it makes it easier for donors to align their ODA programs with the national development plans also in areas other than infrastructure and physical investment.

The process for formulating the CPRGS is also different from the standards used to develop the old central plans. Instead of only expressing the objectives of the central government, the CPRGS is a consensus document that is discussed at a large number of seminars in different parts of the country. Various interest groups, including the donor community, are allowed to present their views and argue for their specific causes. Since the CPRGS has become an integral part of the general 5-year plan, it can be argued that the whole planning process has been changed in the direction of increasing participation from civil society. Even though there is still an ambition to plan the future, there has been a shift in focus from inputs and investments to targets, objectives, and priorities.

What are then the priorities? In its introductory remarks, the CPRGS states eight broad objectives for the country's socio-economic development for the period up to 2010 (SRV, 2003). These are to:

(i) Promote rapid and sustainable economic growth coupled with attainment of social progress and equity.
(ii) Create and equal business environment for all types of enterprises from all economic sectors.
(iii) Continue with structural reforms to bring about a transformation of the nation's economic structure. This objective includes further integration with the international economy and strengthening the competitiveness of Vietnamese industries.
(iv) Provide poor households with opportunities to raise their income by accelerating broad-based growth of agriculture, industry, and services.
(v) Encourage human development and reduce inequality.
(vi) Solve the particular problems of urban poverty with regard to employment, income, and housing.
(vii) Develop and expand social protection and safety net for the poor.
(viii) Undertake public administration reform.

In comparison with earlier strategy documents, there is clearly a stronger emphasis on equity and social issues, although economic growth remains the prime objective. Even if the CPRGS has only been in force for some years, there are already some changes in the pattern of ODA utilization. In particular, there has been a reduction in the share of large-scale infrastructure and an increase in the share of funds directed directly to provinces. Provincial authorities have been given permission to negotiate directly with foreign donors, instead of using MPI as a middleman. Policy and institutional support have emerged as the most important forms of aid. Pro-poor spending, including projects focusing on education, health, and area development, has also increased.

Effects of European ODA

The most important conclusion regarding the impact of European development cooperation with Vietnam is arguably related to the changes in Vietnamese central planning. It is difficult to identify the precise effects of EU's various aid projects on growth and poverty reduction in Vietnam, but it is obvious that the fragmented nature of EU aid has influenced power relations in Vietnamese society. Instead of channeling all ODA through MPI and the central government, individual EU members have sought out local partners and established collaboration with various interest groups throughout the country. This has strengthened the capacity of provinces and line ministries and increased their bargaining power with respect to MPI, which has necessitated changes in the planning process. Instead of a centrally controlled process where resources are distributed to various actors according to the intentions of the central planner economic planning has began to transform into a consultation process that includes large part of society, including the donor community. In the long run, assuming that demands for democratization and human rights will grow stronger over time, this may well be the most important effect of EU aid in Vietnam.

This unintended consequence of aid fragmentation may be a reason to think carefully about what is the optimal degree of aid coordination in countries with authoritarian political regimes. The donor community has for several years stressed the need for stronger aid coordination, and it has also been included as a major objective e.g. in the Paris Declaration on aid efficiency from 2005. However, it is likely that stronger coordination of EU development assistance in Vietnam would mainly have strengthened MPI and the central government, and delayed the necessary reforms of the planning system. It would have allowed Vietnamese authorities to exercise stronger ownership of EU-financed aid projects (which is also a major objective of the Paris Declaration) and might even have resulted in higher aid efficiency, at least as defined by the Vietnamese government's objectives. It is not obvious that this type of development would have been better than what has been achieved with the more fragmented ODA approach of the European Union.

4. Relations with the EU: Trade and Trade Policy

Trade and trade policy are two areas where Vietnam has seen dramatic changes since the introduction of market oriented reforms in the late 1980s. The volumes of imports and exports have increased more than twenty-fold since 1990, with the ratio of trade to GDP exceeding 130 percent during the past five years. This development is explained mainly by policy changes undertaken unilaterally by Vietnam. The market oriented reforms introduced in the late 1980s gradually resulted in a shift from import substitution towards an increasingly export oriented development strategy. The import regime has been cautiously liberalized, with a reduction in the general level of protection and increasing reliance on tariffs rather than quotas, temporary import restrictions, and other discretionary policy interventions.

The donor community has supported both of these policy changes, and several of the largest donors – including the European Union and many of the individual EU countries – have included trade reform as an explicit target in their country strategies for Vietnam. Much of the support for policy reform before 2007 focused on Vietnam's application for WTO membership, although a substantial share of the ODA in infrastructure, industry, and agriculture can also be interpreted as support to internationalization.

Vietnam's trade performance has of course also been affected by the policies of its trade partners – foreign market access has been essential to achieve export success. The most significant event in this area was arguably the lifting of the US trade embargo in 1994. This facilitated a rapid increase in international trade with many countries that had earlier been hesitant to break the embargo, and made it possible for the World Bank and IMF to establish their aid and policy support programs in Vietnam. However, market access has been a problem even after the lifting of the embargo. Not being a member of the WTO until 2007, Vietnam was not guaranteed MFN treatment, and was therefore forced to negotiate bilateral or regional trade agreements with its trade partners to ensure predictable market conditions. As shown in Table 2, by the end of 2004, Vietnam had closed 57 bilateral agreements covering most of its trade relations, including an agreement covering trade with the EU.

Table 2 Number of Bilateral and Multilateral Trade Agreements

	ASIA	AFRICA	EUROPE	AMERICA	Total
Before 1990	1	5	0	0	6
1990-1995	11	2	6	1	20
1995-2000	7	2	3	3	15
2000-2004	4	8	3	1	16
Total	23	17	12	5	57

Source: Ministry of Trade.

A brief look at some of the most important of these trade agreements is useful to illustrate the conditions for Vietnam's internationalization before WTO accession.

ASEAN Free Trade Agreement

Much like the EU, the Association of Southeast Asian Nations (ASEAN) has both economic and political objectives. The political objective is to promote regional peace and stability: at the time of its establishment in 1967, this meant halting the spread of communism from China and Vietnam to other parts of Southeast Asia. The broad economic objective is to accelerate economic growth and social progress in the member states. During the first 25 years of its existence, the organization did not play any significant role in economic affairs. The European Single Market program changed this: the fear that deeper EU integration would lead to protectionism and the establishment of "Fortress Europe" motivated the ASEAN countries to focus more on economic integration. At the Fourth ASEAN Summit in Singapore in 1992 the six member countries (Brunei, Indonesia, Malaysia, Philippines, Singapore, and Thailand) therefore introduced an agreement focusing on deeper economic cooperation. One of the elements of the agreement was the establishment of the ASEAN Free Trade Area (AFTA). The aim was to eliminate tariff and non-tariff barriers on trade between the ASEAN members within a 15-year period.

In 1995, the member countries decided to speed up the integration process, and declared that the regional free trade objective would be met within 10 years rather than the originally stated 15 years. The same year, Vietnam joined the ASEAN and AFTA. Two years later, Myanmar and Laos became members, and Cambodia joined in 1999. By 2003, the six first AFTA members had met their trade liberalization targets and reduced the tariffs on almost all of the goods in their inclusion lists to five percent or below: for nearly two-thirds of the products, the tariff had been eliminated altogether.[2] The four other member countries, including Vietnam, were given longer adjustment periods to meet their AFTA targets. Vietnam met its tariff reduction targets in 2006.

[2] AFTA's trade liberalization scheme is based on a classification of products into three separate lists. The Inclusion List covers the great majority of products: for these tariff lines, the Common Effective Preferential Tariff (CEPT) for intra-regional trade is not allowed to be higher than 5 percent. About 1 percent of all tariff lines, or more precisely, 734 tariff lines, are included in a General Exception List, and are permanently excluded from the free trade agreement for reasons of national security, health, environment, or other historic and cultural values. Finally, member countries can place other sensitive products in a Temporary Exclusion List to facilitate a more gradual adjustment to regional free trade.

In addition to tariff reductions, the AFTA includes rules about the reduction and registration of non-tariff barriers, harmonization of customs procedures, mutual recognition of product standards, alignment of national standards with international standards, and other measures to facilitate trade between the member countries. Like the WTO, it also specifies rules and procedures for the use of emergency measures, and a dispute settlement mechanism for resolving problems related to the implementation of the agreements.

The AFTA agreement has been important for opening the regional market to Vietnamese exporters, and promoting reforms of Vietnam's own trade policies. Thanks to the trade preferences, Vietnam was able to quadruple its exports to the other ASEAN countries between 1995 and 2005, from $1 billion to $4 billion. However, the size of the ASEAN market is small relative to the US, the EU, and Japan, and Vietnam's exports are often competitive rather than complementary to the exports of other ASEAN countries. This means that although Vietnam has been able to enter the regional market on favorable terms, exports to the ASEAN countries are less important than exports to developed market economies.

United States

The economic relations between Vietnam and the US were frozen from the end of the war in 1975 until 1994, when the US trade embargo was lifted. Although the trade and investment relations between the two countries grew steadily from that time, the US remained a relatively small trade partner until 2000, when a comprehensive bilateral trade agreement (BTA) was signed. The BTA, which came into force in late 2001, outlined a WTO-type framework covering not only tariffs, but also a host of other areas where Vietnam would need to undertake substantial reforms. Apart from promises to extend MFN and national treatment privileges to the partner country, the agreement included rules on trade related investment measures (TRIMs), trade related intellectual property rights (TRIPs), trade in services, technical barriers to trade, and various other commitments related to transparency, customs valuation, and business facilitation.

Since the US already fulfilled most of these requirements, the BTA put particular demands on Vietnamese legislation, which had relied to a large extent on licenses, quotas, and other discretionary interventions during the 1990s. Some of the required changes were immediate, but in other cases Vietnam was given an adjustment period until 2005 or 2006 to reform rules and policies. Hence, the BTA forced Vietnam to adopt much of WTO law already before accession to the WTO. In some instances – e.g. investment and business facilitation – the BTA actually went further than WTO, which does not have any provisions in these areas (aside TRIMs). In other cases, the BTA was less stringent than the WTO. In particular, although the agreement included rules about the use of safeguards, countervailing duties, and antidumping tariffs, it did not specify legal standards, rules on investigations, or procedures to challenge actions in these areas. The WTO, by contrast, has a well developed dispute settlement procedure that allows members to challenge allegedly WTO inconsistent actions of other members.

Regarding the level of protection, the BTA required Vietnam to lower its tariffs in several hundred tariff lines (mainly agricultural products) that were considered important for US business. It did not oblige the US to reduce specific tariffs, but required the US to include Vietnam among the countries eligible for GSP tariffs. This was a substantial improvement compared to the situation before the BTA: the average tariff for Vietnamese exports fell from about 40 percent to four percent. One result of the BTA has been a very rapid increase in the trade between Vietnam and the US. Vietnam's exports to the US grew from $170 million in 1995 to $800 million in 2000 and more than $6.6 billion in 2005. The importance of the US has continued increasing since Vietnam's entry into the WTO, and exports reached 12.3 billion in 2009. Meanwhile, imports from the US grew from about $180 million to $3.1 billion over the same period.

European Union

Vietnam and the EU established diplomatic relations in 1990, after the Vietnamese withdrawal of troops from Cambodia, and a series of trade agreements have followed since that time. An agreement on trade in textiles (connected to the MFA) was closed in 1992, a more comprehensive framework agreement on trade and economic cooperation was established in 1995, and the trade agreement was revised in 2004 when Vietnam and the EU completed the bilateral negations related to Vietnam's WTO membership application. The agreement granted EU members MFN treatment in the Vietnamese market, while Vietnam was given access to EU's GSP tariffs, which are often substantially lower than MFN tariffs. The European GSP tariffs are classified in four categories depending on how sensitive the products are considered to be. For the most sensitive items in the GSP lists, including mainly agricultural products, the preferential tariffs are about 15 percent lower than the MFN tariffs, leaving substantial trade barriers protecting European producers. In particular, the escalation of tariffs leaves high levels of protection for processed food products, making it difficult for developing countries to move into higher value added activities. For less sensitive products, mainly manufacturing products, GSP tariffs are lower, in many cases fixed at zero. These preferences have been maintained also after Vietnam's accession to the WTO.

Yet, although GSP tariffs are lower than MFN tariffs, it is hard to determine how much of a competitive advantage they provide for Vietnam. Firstly, EU's average MFN tariffs are already low, at about four percent for manufacturing products, which leaves little room for preferences. Secondly, almost all countries have more favorable access to the EU market than what is provided by the MFN rules. A few years ago, the US, Canada, Japan, Australia and New Zealand were the only countries that only had MFN treatment: in the last couple of years, this list has been extended with Hong Kong and China, Singapore, Taiwan, and South Korea, who have graduated from the GSP system. Thirdly, ACP countries and LDCs have access to even more beneficial trade rules through the Cotonou Agreement and the EBA Agreement. There are also rules of origin and other restrictions (such as technical standards and phytosanitary regulations) that make it difficult to fully use the preferences, particularly in the food industries. This notwithstanding, Vietnam has been very successful in reaching the EU market, and exports to the EU grew from about $600 million in 1995 to nearly $11 billion in 2008, making EU the top export destination next to the US.[3]

World Trade Organization

[3] Japan was the most important OECD export market for Vietnam through most of the 1990s, but has fallen back to the third position during the past half-decade. In 2008, Vietnam's exports to Japan amounted to about $8.5 billion. The trade relations are governed by a trade agreement from 1999, which is in many ways similar to Vietnam's agreement with the EU. Japan is guaranteed MFN treatment in the Vietnamese market, while Vietnam has access to Japanese GSP tariffs.

Although Vietnam has completed a large number of bilateral trade agreements during the past 15 years, it can still be argued that Vietnam's long-lasting negotiations with the WTO have been at the center of the trade policy agenda during most of this period. Vietnam applied for WTO membership already in January 1995, and the accession negotiations in the WTO Working Party progressed concurrently with various bilateral negotiations from 1998. Several of the bilateral agreements, including those with the US and the EU, were actually parts of the preparation for WTO membership. In the US case, it is clear that most of the BTA rules were modeled on the WTO, and a substantial share of the adjustment to the WTO was achieved simply by extending BTA treatment to other member countries. The 2004 trade agreement with the EU was even more directly connected to the WTO, since it resulted from the bilateral negotiations in the WTO accession process.

In May 2006, Vietnam reached a bilateral "agreement-in-principle" with the US, completing the negotiations with 28 WTO Working Party members and clearing the way for a final accession bid.[4] Vietnam formally joined WTO in early 2007. Vietnam's history as a planned economy is one reason why the accession process was slow and complex. The WTO is based on market principles and it has been difficult to integrate its rules and regulations into Vietnam's existing legal framework, which is largely obsolete. Another problem was the privileged position of SOEs, which is not consistent with rules about national treatment and non-discrimination. Another reason was the size of Vietnam's Working Party. The fact that 68 countries decided to take part in the negotiations suggests that many observers expect Vietnam to become a significant actor in the future. Vietnam's trade partners have therefore been concerned about future competition from Vietnamese companies, arguing that safeguards against rapid Vietnamese export expansion are needed, at the same time as they have pressed for improved access to Vietnam's domestic market, particularly in the service sector. It is obvious that these views were not always easy to reconcile with Vietnam's wish to reform slowly and maintain a leading role for the state. Considering Vietnam's apparent success in securing reasonably good access to the most important foreign markets through bilateral agreements, it is therefore relevant to ask why it spent so much time and effort to be accepted as a WTO member. There are at least three arguments that have appeared in the Vietnamese debate.

Firstly, even though bilateral agreements have provided good market access, they were considered as less predictable than WTO membership. In particular, bilateral agreements did not automatically adjust to the progress made in multilateral agreements. For instance, not being a WTO member, Vietnam could not automatically benefit from the abolishment of garment quotas that resulted from the termination of WTO's Agreement on Textiles and Clothing on January 1, 2005. Most of Vietnam's important trade partners did lift the quotas on Vietnamese clothing exports as well, but this was generally done on the basis of unilateral decisions that might be reversed later on. As a WTO member, Vietnam would have been able to request the same treatment in all trade related areas as other WTO members.

Secondly, some of Vietnam's bilateral trade agreements were subject to regular review and could be cancelled or changed because of arguments not related to trade. For instance, Vietnam did not have unconditional "normal trade relations" with the US. The Jackson-Vanek amendment of the

[4] In total, 68 countries participated in the Working Party, but only 28 (including the EU, representing its 25 member states) requested bilateral negotiations.

Trade Act of 1974 restricts trade with countries that do not fulfill US definitions of “freedom of emigration”, and the US President had to grant an annual waiver for Vietnam in order to allow Vietnamese products to enter on MFN terms. With WTO membership, Vietnam gained permanent normal trade relations.

Thirdly, although many of Vietnam’s bilateral agreements outlined rules for the use of trade remedies (safeguards, countervailing duties, and antidumping tariffs) there were seldom any rules or procedures for dispute settlement. For instance, Vietnam could not challenge US or EU decisions about antidumping tariffs outside the US or EU court systems. As a WTO member, Vietnam has access to WTO’s dispute settlement system, where qualified expert panels make impartial assessments of complaints, with strict time schedules for the various stages of the dispute settlement process.

The general perception in Vietnam is that the need for a functioning dispute settlement system has increased over time. As long as Vietnam was a weak exporter, it did not pose any threat to local industries in foreign markets, and foreign governments could afford to provide generous rules for market access. As Vietnam has gradually grown to become a stronger competitor, with notable market shares in some sectors, the implementation of rules has become less generous and the need for a functioning dispute settlement system has become more obvious.

WTO accession has provided a stronger and more predictable position for Vietnam in foreign markets, but it has also required other reforms of Vietnamese trade rules. One step concerns the extension of many of the provisions in the US BTA to all other WTO members. In addition, Vietnam has been forced to improve market access – the average tariffs have fallen substantially – and deepen commitments in several areas. The BTA required that about 4 percent of Vietnam’s tariffs would be bound, but WTO has required binding all tariffs. Vietnam has added new commitments regarding the use of technical barriers to trade and rules of origin, WTO’s agreement on trade in services (GATS) is more comprehensive than the BTA, there are additional provisions on trade-related intellectual property rights (TRIPS), and the agreement on agriculture calls for stronger discipline in the use of state aid and export subsidies. Moreover, Vietnam has conformed to the WTO rules for the use of trade remedies. Most of these provisions benefit Vietnamese business and consumers as well as foreign exporters: in particular, lower levels of protection, increasing transparency, and higher predictability have clearly promoted investment, growth, and development in areas where Vietnam has comparative advantages.

The agreement also included some safeguards that can be considered troublesome. For instance, Vietnam was forced to accept to be designated as a “non-market economy” for a substantial period after accession – until 2018. This is a potential problem if any one of Vietnam’s trade partners decides to apply antidumping tariffs on Vietnamese exports. The domestic price structure in a country categorized as a “non-market economy” is assumed to be so distorted that it is impossible to use domestic prices to determine whether the country is dumping goods. Instead, the cost calculations needed to determine whether there is dumping (and how high antidumping tariffs should be) can be based on cost calculations from third countries. Given the relatively strong competitiveness of Vietnamese exporters in labor and resource based industries, it is always possible to find third countries where costs are larger than the Vietnamese prices – in other words, Vietnam is highly vulnerable to antidumping accusations, and is not able to rely on

WTO's dispute resolution mechanism to challenge partner countries that decide to impose antidumping duties on Vietnamese goods.[5]

Summarizing the development of Vietnamese trade policies and the trade policy environment in which Vietnamese exporters operate, it is safe to conclude that the changes in recent years have been conducive to development. Vietnam's own trade policies have been simplified and liberalized, which has reduced the distortions caused by the import substituting policy that characterized the economy until the late 1990s. Foreign countries have been willing to provide market access on favorable terms, creating a potential for export-led growth. The total volume of exports has increased rapidly, and the export structure has become more diversified, with a shift from primary products to manufacturing. Import capacity has grown accordingly, allowing Vietnam to use foreign technologies and intermediate products to upgrade its production structure and accelerate the rate of industrial development. Moreover, the developments in the trade arena have been essential for creating a favorable environment for FDI – in recent years, Vietnam has been able to attract very substantial amounts of foreign investment, as noted in Table 1.

Interactions between ODA and Trade

The discussion in the previous two sections suggests that there is substantial coherence between the aid and trade policies of many of the donor countries that are active in Vietnam. The policy advice given by donors has stressed the need for trade reform, both in order to promote exports and to reduce the distortions caused by protectionism. Accordingly, ODA resources have been used directly to promote trade reform – including support to Vietnam's application for WTO membership – and indirectly to ease the costs caused by trade reform and to improve the competitiveness of Vietnamese exporters and import-competing firms.

At the same time, most donor countries have been reasonably generous in providing market access for Vietnamese exporters. Unlike most other developing countries, Vietnam did not have any automatic market access or MFN guarantees in foreign markets before its WTO accession in 2007. Instead, in their bilateral market access negotiations, Vietnam's trade partners have been able to decide what level of trade preferences they want to extend to Vietnam. In most cases, the choice has been to allow Vietnamese goods to enter on GSP terms. This relatively favorable treatment has facilitated a rapid increase in exports, which in turn has had a strong positive effect on Vietnamese development. The main exception is processed agricultural products, where many export destinations remain highly protected. The access to foreign markets has made Vietnam an attractive location for efficiency-seeking FDI, facilitated various contacts that have contributed to technology transfer and learning effects, and generated hard currency earnings that have been translated into substantial import capacity.

In addition to discussing the relationship between aid and trade policies of the donors and noting that ODA flows may interact with the trade policy of the recipient country, Suwa-Eisenmann and Verdier (2006) identify a number of other effects in the ODA-trade locus that may be important for development. Some of these are less acute in the Vietnamese case than in many other cases.

[5] Several countries, including the ASEAN members, Australia, New Zealand, India, and Argentina, have granted Vietnam market economy status, but the US, EU, and Japan still consider the country a non-market economy.

For instance, issues related to aid dependency and terms-of-trade effects are not very critical in Vietnam, given that aid makes up a relatively small share GDP: as noted above, the ratio of ODA to GDP has been around 4 percent, and it is likely to fall in the future. One reason is the high growth rate of the economy, which means that an unchanged amount of aid constitutes a smaller and smaller share of GDP. Another reason is that Vietnam has reached an average income level of $1,000 per capita, which is likely to lead to a reduction in some forms of aid (mainly grants). It is also likely that some bilateral donors will reduce their contributions to Vietnam as they shift focus to countries where the success in social and economic development is more limited – a case in point is Sweden, which has already reduced funds for bilateral development cooperation. A third reason is that the inflows of FDI and private transfers are both larger than ODA, and will probably remain so.

Another issue that is not very complicated in the case of Vietnam is the causality between aid and trade. Given the lack of commercial contacts between Vietnam and its donors before the early or mid-1990s, it is obvious that aid has preceded trade in most bilateral cases. The question whether "aid or trade" is more important also appears less controversial in Vietnam than in many other developing low-income countries, particularly if present trends are extrapolated. Somewhat crudely, it can be argued that the Vietnamese economy would suffer more severely if market access in donor countries was limited than if ODA flows were terminated.

Development over time: from aid recipient to competitor

Many of the bilateral trade relations between Vietnam and the OECD countries were established at a time when Vietnam's export capacity was low, and Vietnamese producers could not pose any threat to local firms in foreign markets. Hence, providing generous rules for market access was not very costly, but could be politically convenient, both with regard to domestic interest groups and in an international context. Over time, however, the situation has changed as a result of Vietnam's increasing export capacity and the diversification of Vietnam's exports. As Vietnamese firms are beginning to take advantage of the market access preferences in their partner countries, they are also beginning to cut into the market shares of local firms.

Consequently, Vietnam's increasing export competitiveness has begun to cause friction in some foreign trade relations. Most of Vietnam's bilateral trade agreements include rules for the use of trade remedies, such as safeguards and antidumping tariffs, and they have also been used with increasing frequency. As seen in Table 3, Vietnam was subject to five trade conflicts with foreign countries between 1994 and 2001, three of which resulted in the imposition of antidumping tariffs. Between 2002 and 2008, the frequency of trade disputes increased dramatically, with 22 new cases initiated by Vietnam's trade partners, several by the European Union and the US. After the onset of the global financial crisis, there has been another distinct increase in the number of antidumping complaints, with 14 new cases filed against Vietnam between August 2008 and March 2010.

Table 3 **Trade Disputes 1994-2008**

No.	Year	Product	Country	Conclusion
1.	1994	Rice	Colombia	No antidumping tariffs applied – no harm to local rice producers shown.
2.	1998	Glutamate	EU	Antidumping tariff of 16.8%.
3.	1998	Shoes, sandals	EU	No antidumping tariff applied – small market share.
4.	2000	Gas lighters	Poland	Antidumping tariff of EUR 0.09/lighter.
5.	2001	Garlic	Canada	Antidumping tariff of $1.48/kg.
6.	2002	Shoes and soles	Canada	No antidumping tariff applied – no harm to local producers shown.
7.	2002	Lighters	South Korea	Complaint withdrawn.
8.	2002	Lighters	EU	Complaint withdrawn.
9.	2002	Catfish	USA	Antidumping tariffs of 36.84-63.88%.
10.	2003	Zinc oxide	EU	Antidumping tariffs of 93%.
11.	2003	Chains	EU	Antidumping tariff equal to difference between EUR325/1000 chains and price stated in the invoice.
12.	2003	Shrimp	USA	Antidumping tariff of 4.3-25.7%.
13.	2004	Motorcycle and bicycle tubes /tires	Turkey	Antidumping tariffs of 29-49%.
14.	2004	Bicycles	EU	Antidumping tariffs of 15.8-34.5%.
15.	2004	Steel pipes and steel goods	EU	No antidumping tariffs imposed.
16.	2004	Stainless steel fasteners	EU	Antidumping tariff of 7%.
17.	2004	Fluorescent lamps	EU	Antidumping tariff of 66.1%.
18.	2004	Surfboards	Peru	Antidumping tariff of USD 5.2/unit.
19.	2005	Leather shoes	EU	Antidumping tariff of 16.8% from July 2006.
20.	2005	Fluorescent lamps	Arab Union	Antidumping tariff, USD 0.32/unit.
21.	2005	Bicycle spokes	Argentina	Antidumping tariff of 81%
22.	2006	Driving belt	Turkey	Antidumping tariff, USD 4.55/kg.
23.	2006	Fabric footwear	Peru	
24.	2007	Gas lighter	Turkey	
25.	2007	Fluorescent lamps	India	
26.	2007	CD-R	India	Antidumping tariff, INR 3.04-3.23/unit
27.	2008	Uncovered innerspring	US	
28.	2008	Flat yarn of polyester	India	

Source: Ministry of Trade, Hanoi, personal communication; Le and Tong (2009).

In most of the dispute cases, Vietnam has denied dumping, and argued that the low prices of its products were due to low labor costs and other sources of comparative advantages. These arguments have rarely been successful, and over 70 percent of the disputes have resulted in the imposition of antidumping tariffs on Vietnamese exporters. One reason is that Vietnam has had a weak bargaining position in the dispute resolution processes. Antidumping complaints are treated as domestic cases in the courts of Vietnam's trade partners – before 2007, Vietnam's bilateral trade agreements did not include provisions for impartial dispute settlement of the kind found in the WTO. Instead, Vietnam was restricted to challenging the antidumping decisions of its trade partners in the courts of the partner countries, according to the specific laws of those countries.

The accession to the WTO did not result in any great improvement of the Vietnamese bargaining position. As noted earlier, the accession agreement defined Vietnam as a "non-market economy", which means that importing countries can claim that there is dumping as soon as Vietnamese firms charge prices that are lower than those in "comparable" market economies. For instance, the EU's decision to levy antidumping decisions on imports of Vietnamese leather shoes was based on cost and price comparisons with Brazilian shoe producers.[6] Similarly, the large catfish and shrimp conflicts with the US were based on arguments that Vietnam's non-market economy status provided unfair advantages to Vietnamese producers.

While some industries still benefit from public support that is not compatible with fair trade arguments (e.g. shipbuilding, where the state-owned Vinashin has received substantial amounts of state-guaranteed credit on unclear terms), most private enterprises do not, and it is clear that these regulations may constitute a formidable obstacle for Vietnamese export companies in the future. The problem, from the Vietnamese perspective, is that individual private companies can be subject to antidumping remedies even if there is no challenge against their individual pricing decisions or business practices: instead, the grounds for antidumping tariffs may be that Vietnamese land prices or electricity prices are not market-determined, or that labor costs do not reflect the underlying market conditions. This is likely to have harmful development effects. Although there are no detailed analyses of the consequences for Vietnam of foreign antidumping actions, it is possible to identify two likely outcomes. Firstly, the imposition of tariffs raises the price of Vietnamese products, which reduces sales, production, and incomes in Vietnam. Given that most of the industries and product groups involved in trade disputes are labor-intensive, the costs in terms of employment can be substantial. For instance, Vietnamese industry sources estimate that the EU tariffs on leather shoes resulted in tens of thousands of lost jobs even before they were introduced, since EU customers cancelled orders in anticipation of the antidumping tariff. The effects on poverty are likely to be severe: most of the workers in the labor-intensive industries have low levels of education, but earn salaries that are substantially larger than the earnings in agriculture or the informal sector.

Secondly, the threat of antidumping tariffs will affect competition and pricing decisions. This is a particularly severe problem for the cases where the antidumping claims are based on "non-market economy" arguments. Instead of following normal business principles, where products are priced on the basis of demand conditions and production costs, Vietnamese producers may be forced to engage in strategic behavior, where one objective may be to limit growth rates and

[6] The antidumping case involving leather shoes was initiated before Vietnam joined the WTO, but the EU applied a non-market economy rule for Vietnam already before that time.

market shares in order to avoid the imposition of trade remedies. A possible consequence is the emergence of export cartels to coordinate the behavior of the individual firms. An alternative outcome is stronger state intervention and export controls on the Vietnamese side. Both these outcomes are undesirable from a development perspective. The development of an export cartel is likely to affect competition in the domestic market as well, limiting growth and raising prices for local consumers. A solution where the degree of state interference increases because of trade policy concerns is also highly undesirable, and in stark contrast with the general trend in Vietnamese economic development, where private enterprise and market determined decisions are promoted.

Can the EU live with successful developing countries?

The WTO accession clause designating Vietnam as a non-market economy until 2018 is one of the clearest examples of a situation where the trade policies of Western countries, including the EU, are in obvious disagreement with ODA and development policies.[7] While ODA and the development dialogue in general promote an increasing market orientation, trade policies freeze Vietnam's status as a non-market economy for an extended period, without any regard for what happens in Vietnam. A likely consequence is that the momentum for domestic reform is weakened: the argument will be "Why reform if our reforms are not recognized by our trade partners?" The EU has decided not to follow Australia, New Zealand, and several other countries that have recognized Vietnam as a market economy. Should this be interpreted as a new stage in the relations between the EU and Vietnam – a stage that is better characterized by competition and conflict rather than cooperation?

Although Vietnam is a rapidly developing country that may be expected to play an increasingly important global role in the future, there is still a long way to go before this potential is realized. At present, Vietnam is a small economy – in spite of its 90 million inhabitants, it has a nominal purchasing power that is smaller than that of a medium-sized European city like Stockholm or Copenhagen, and accounts for less than 0.7 percent of EU imports. There is little scope for claiming that Vietnam could pose a serious competitive challenge to the EU, except in very narrowly defined industrial sectors. Hence, it is unlikely that conflicts and competition related to trade and economic relations could motivate a shift in the EU's relationship with Vietnam at this time.

This positive statement appears to contradict the picture suggested by the EU's use of antidumping tariffs against Vietnam and the Union's unwillingness to recognize Vietnam as a market economy. This apparent contradiction is probably explained by the relation between the EU and China. Whereas Vietnam does not pose any significant challenge to European firms, there is no doubt that China does. Chinese exporters have captured dominant positions in a wide range of manufacturing industries and account for 27 percent of the EU's imports of manufacturing goods. Moreover, trade with China exhibits large imbalances, with the EU deficit reaching nearly EUR 220 billion in 2008 – only about EUR 13 billion less than the US trade

[7] In extreme cases, Vietnam's trade partners might refer to the non-market economy clause if Vietnamese exporters rely heavily on ODA-financed infrastructure, or benefit from technical advice, financing, or other business services provided through aid-financed programs. It is also interesting that the general view in the development economics literature is that non-market conditions constitute a general disadvantage rather than a competitive advantage. By contrast, trade legislation accommodates the view that non-market conditions could create advantages in all sectors.

deficit with China. Understandably, the EU is concerned about competitiveness, employment, and macroeconomic balance in its relations with China.

This concern spills over to the relationship with Vietnam. One reason is the similarity in history and economic structure between China and Vietnam. Both countries have a past as planned economies, and both operate state-dominated market economies where state-owned enterprises play important roles. It will be difficult for the EU to motivate different treatments of Vietnam and China in a WTO context: given that China is more important, it is clear that the common policy approach will mainly focus on China. Hence, it is unlikely that the EU will unilaterally revise Vietnam's non-market economy status.

Moreover, Vietnam and China are linked when it comes to current trade and investment patterns. Several of the antidumping tariffs faced by Vietnam are brought about by these links. Bicycles, leather shoes, and fluorescent lamps are examples of cases where the EU has first initiated antidumping proceedings against China, and where the Chinese producers (or foreign investors operating in China) have subsequently moved to Vietnam.[8] In cases where this migration of production has not occurred, Vietnam has generally not been subject to the same trade remedies as China. For example, comparing the frequency of antidumping actions, it is notable that China was targeted by the EU 122 times during the past decade, whereas Vietnam was named only 9 times.[9] Another notable observation is that the EU has refrained from levying any new antidumping tariffs on Vietnam after 2006 (but the tariffs on Vietnamese leather shoes have been extended during this period), although the global financial crisis has contributed to a distinct increase in the use of trade remedies during the last two years.

A cautious conclusion from these observations is that the relationship between the EU and Vietnam is still amicable, in spite of the rapid growth in Vietnam's economy and the increasing strength of Vietnam as an export base: the parental relationship from the 1990s has not been replaced by a distinctly more competitive one. This favorable link is to some degree obscured by the European need to manage the more competitive relation with China – overall, it will be difficult to provide special preferences to Vietnam. The exception from this generalization is the ongoing negotiation between the EU and Vietnam regarding a preferential trade agreement. Although restrictive rules of origin will probably limit the ability of Vietnam to utilize the trade preferences under this type of agreement, it would still provide distinct structural benefits to Vietnam. Most importantly, it would make it possible for the EU to recognize Vietnam as a market economy without having to extend the same treatment to China. In addition, it would include an investment agreement that would make Vietnam a more attractive location for European investors. The outcome of these negotiations are of great interest not only for the EU and Vietnam, but also for other developing countries and emerging markets that worry about the possibilities to pursue export oriented development strategies, with the EU as a major export destination. A successful result will demonstrate that the EU's trade preferences towards developing economies are not only temporary promises that will be deflated if the partner economy is actually able to achieve sustained growth and create the capacity to utilize the preferences.

[8] See http://www.vnnnews.net/anti-dumping-mud-sticks-on-firms.
[9] For data on EU antidumping cases, see http://trade.ec.europa.eu/doclib/docs/2010/january/tradoc_145673.pdf.

5. Concluding comments

The relationship between the EU and Vietnam is currently in a process of change. The rapid development of the Vietnamese economy is altering the basic setting for the interactions between the two regions. As long as Vietnam was a weak developing economy with limited capability for internationalization, the EU's contacts with Vietnam were mainly related to development aid. Both the EU commission and more than a dozen member countries had bilateral aid programs in Vietnam, with various specific targets depending on the overall policy preferences of the individual donors. The general objective was to promote sustainable growth and progress in social development. Like all other aid relationships, it could be argued that this relationship was to some extent "paternal", in the sense that that it involved more developed partner that contributed both physical resources and knowledge about "development" to a less developed partner. However, because of historical reasons, Vietnam was concerned about the risk that external powers might interfere with domestic affairs and established a structure for aid management that would guarantee Vietnamese ownership of the country's development agenda. Aid was made into an integral part of the economic planning process and aid management was centralized to the Ministry of Planning and Investment. The possibility to use aid and explicit conditions in order to influence Vietnamese policy was limited.

Still, the EU's ODA investments turned out to have a fundamental impact on the Vietnamese economy, although not in a manner that was explicitly intended by the EU. The fragmentation of the Union's aid portfolio into more than 15 different bilateral programs, each made up of several components, meant that the Vietnamese government centralized responsibility for a large share of the ODA projects to regional and sectoral authorities. Over time, this contributed to increasing the relative strength and bargaining power of actors outside central government, and led eventually to thorough reforms of the central planning system: it became impossible to impose a central plan when various regional and sectoral authorities could act independently to secure promises of external resources from the donor community.

More recently, Vietnam has started to develop notable export capacity and increased its attractiveness as a low-cost production location for foreign multinational enterprises. The emergence of Vietnamese products in the European marketplace has coincided with a designation of Vietnam as a "non-market economy" and the introduction of European antidumping tariffs against selected Vietnamese exports – goods like bicycles, leather shoes, and fluorescent lamps. This implies that the European attitudes towards Vietnam may have changed, so that the focus on supporting Vietnamese development through ODA has been replaced by a more complex relationship, where Europe feels a need to protect its markets from competition from Vietnam. Yet, there is reason to believe that the bilateral relationship must not necessarily deteriorate towards a more competitive and antagonistic association. The reason is that the protectionist reactions from the European side are probably not focused primarily on Vietnam, but rather on China. Several of the antidumping cases brought against Vietnam are extensions of cases initiated against China, and the designation of Vietnam as a non-market economy follows a similar policy with respect to China. The current negotiations about a preferential trade agreement between the EU and Vietnam could, if concluded successfully, cement a more positive relationship. Such a development would also signal to other developing countries that good relations with the EU are possible even when emerging economies are successful enough to win market shares in the European market. That would be a highly encouraging signal in a world where many other developments suggest a stronger polarization between different growth centers and spheres of interest.

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