

Diplomat
12 July 2019

A Deeper Look at Vietnam's Trade Deal With Europe

The EU's drive to become the defender of multilateralism promises further opportunities for Southeast Asia.

By Stuart Brown

On June 30, Vietnam signed a trade agreement and investment protection agreement with the European Union (EU). In doing so, the country became the second member of the Association of Southeast Asian Nations (ASEAN), following Singapore, to conclude a major trade agreement with the EU. Although the news was partly upstaged by the EU's agreement with the South American trade bloc Mercosur just a few days earlier, the deal has important implications not only for Vietnam's relationship with Europe, but for the EU's wider role in Southeast Asia.

Economic and Political Gains

There are obvious economic benefits for both sides, with a 99 percent reduction in tariffs envisaged. From day one, around 65 percent of EU exports to Vietnam will be tariff free, with most other areas being fully liberalized over the next 10 years. For Vietnamese exports to the EU, 71 percent of exports will be tariff free from day one, with 99 percent liberalized within seven years.

Just as importantly from the European perspective, the deal allowed the EU to further strengthen its credentials as the chief defender of free trade and multilateralism, at a time when the protectionist instincts of Donald Trump and an entrenched trade conflict between the United States and China continue to dominate global affairs.

Indeed, the contrast between the approach pursued by Trump in Vietnam and the deal with the EU could hardly have been greater. In the days leading up to the agreement, the U.S. president had sharply rebuked the country, labeling Vietnam "almost the single worst abuser of everybody." Trump's ire, as ever, was linked to a burgeoning trade deficit between the United States and Vietnam.

Ironically, the China-U.S. trade conflict has been one of the main precipitating factors for this. As the Wall Street Journal explains, "while Chinese goods exports to the U.S. fell 12.3% year-over-year from January through May, Vietnam saw a 36.4% increase," with Vietnamese exporters drawing impetus from the redirection of trade and changing supply lines. A recent analysis by the Japanese investment bank Nomura found that Vietnam had been the largest winner from the conflict so far, with trade diversion equating to a gain of 7.9 percent of GDP. Taiwan was the second biggest beneficiary from trade diversion, with gains of around 2.1 percent of GDP.

Vietnam has thus not only gained directly from the China-U.S. trade conflict, but also now stands to benefit through its deal with the EU, brought in part by Europe's desire to fill the vacuum left by the United States as the foremost advocate of free trade. In recent months, EU trade commissioner Cecilia Malmström has been increasingly blunt about the EU's ambitions in this context. Summing up the deal with Vietnam, she was

unequivocal, stating that Europe had sent “a very powerful signal that says, ‘we believe in trade.’”

An Outward Looking Europe

The United Kingdom’s impending exit from the European Union, which is due (though by no means guaranteed) to take place by the end of October, has also provided fresh motivation for Europe to establish new partnerships. There are real concerns the U.K. could leave the EU without negotiating a replacement deal and in the process damage both the British and European economies.

But the EU’s push to conclude trade agreements as a response to Brexit is as much about politics as it is about economics. A key argument advanced by those who campaigned for the U.K.’s withdrawal was that by removing itself from the EU’s customs union, the country would be able to negotiate its own bespoke deals across the world. This constituted a direct challenge to one of the primary rationales for the EU’s existence: the benefits of pooling sovereignty as a trade bloc. It is little surprise European leaders have redoubled their efforts to conclude trade agreements ever since.

Hence both external opportunities generated by the China-U.S. trade conflict and internal challenges are now motivating the EU to reach deals around the world. Meanwhile economic realignments are pushing European companies toward Asian markets. Alongside Vietnam and Mercosur, a deal with Japan entered into force in February. The EU’s long-term goal in Southeast Asia is to use bilateral deals with ASEAN members to work toward a region-to-region free trade agreement. Following Singapore and Vietnam, the next likely target will be Indonesia.

Yet for new deals to be agreed, the EU will need willing partners. EU relations with Indonesia and Malaysia have been significantly undermined by the fallout over a proposed EU ban on the use of biofuels made from palm oil. Around 40 percent of imported palm oil in the EU is used as fuel, a legacy of earlier EU targets that sought to encourage the adoption of transport fuels derived from renewable sources. The proposal to phase out the use of palm oil-derived biofuels was motivated by concerns over deforestation, but with Indonesia and Malaysia accounting for over 80 percent of global palm oil production, the prospects of a breakthrough on trade have rapidly diminished.

Meanwhile the U.K., for its part, may soon be looking to establish its own negotiations with ASEAN states if and when it leaves the EU. By virtue of its EU membership, the U.K. is a participant in around 40 trade deals covering over 70 countries across the world. It is an open question as to whether it will be possible to roll over many of these agreements, including the one concluded with Vietnam, following Brexit, or whether London will be obliged to negotiate new deals from scratch, potentially with less beneficial terms. In June, the U.K. managed to conclude its first post-Brexit trade agreement in Asia when it reached a preliminary deal with South Korea, broadly replicating the terms of the existing EU-South Korea free trade agreement.

Balancing Values Against Economic Interests

The palm oil affair underlines one of the fundamental dynamics at the heart of EU trade policy. While many European actors view trade deals simply as tools for furthering economic interests, others argue that trade concessions should be used as incentives for achieving value-oriented goals, such as bolstering environmental protection and human

rights. This balancing act has an expression in most of the EU's external relations throughout the world, from Southeast Asia to the Arctic.

It is far from a niche concern given EU trade deals remain vulnerable to opposition in the European Parliament if they are seen to shirk on the promotion of EU values. The EU's deals with Mercosur and Vietnam will both have to pass through the Parliament if they are to be ratified, and this will be no mere formality.

Green parties, aided by a strong result in the European Parliament elections in May, have already criticized the Mercosur deal for falling short on the environment. Philippe Lamberts, co-leader of the Green bloc in the Parliament, recently derided sustainability provisions in EU trade deals as "a joke" on the basis that they are typically not accompanied by viable sanctions. In the case of the deal with Vietnam, human rights concerns have formed the main focus for opposition. Expectations are the agreement will be ratified, but previous experiences, such as the mini-crisis over the EU's free trade deal with Canada, serve to illustrate the potential perils of ratification.

Regardless of what happens next, Vietnam has proven to be a major winner from recent developments in global trade. It may not be the last. But whether other Southeast Asian states will follow the country in reaching a deal with the EU will depend to a sizable extent on squaring economic interests with the EU's desire to use trade as a mechanism for projecting its values across the world.

Stuart Brown is a research associate in the European Institute of the London School of Economics and the Managing Editor of EUROPP – European Politics and Policy