World Trade and Vietnam - An Overview

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Intermediate Microeconomics II

Fulbright Economics Teaching Program – MPP8

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Outline

- Largest trading partners of the Vietnam
  - Top Importers
  - Top Exporters
- Gravity model:
  - influence of an economy's size on trade
  - distance and other factors that influence trade
- Borders and trade agreements
- Globalization: then and now
- Changing composition of trade
- Service outsourcing

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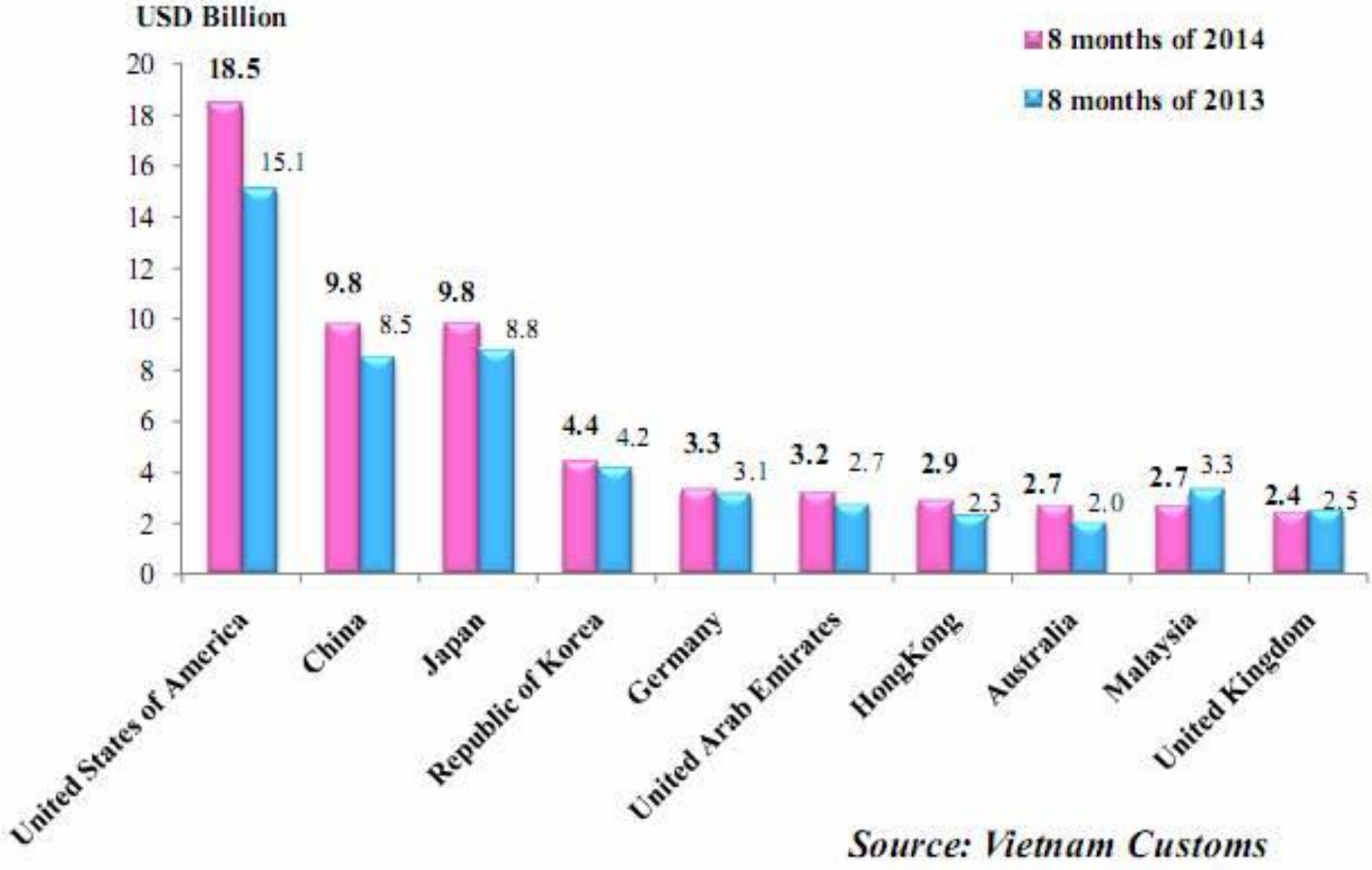
Chart 1: Top 10 main exporting markets of Vietnam in the 8 months of 2014



Source: Vietnam Customs

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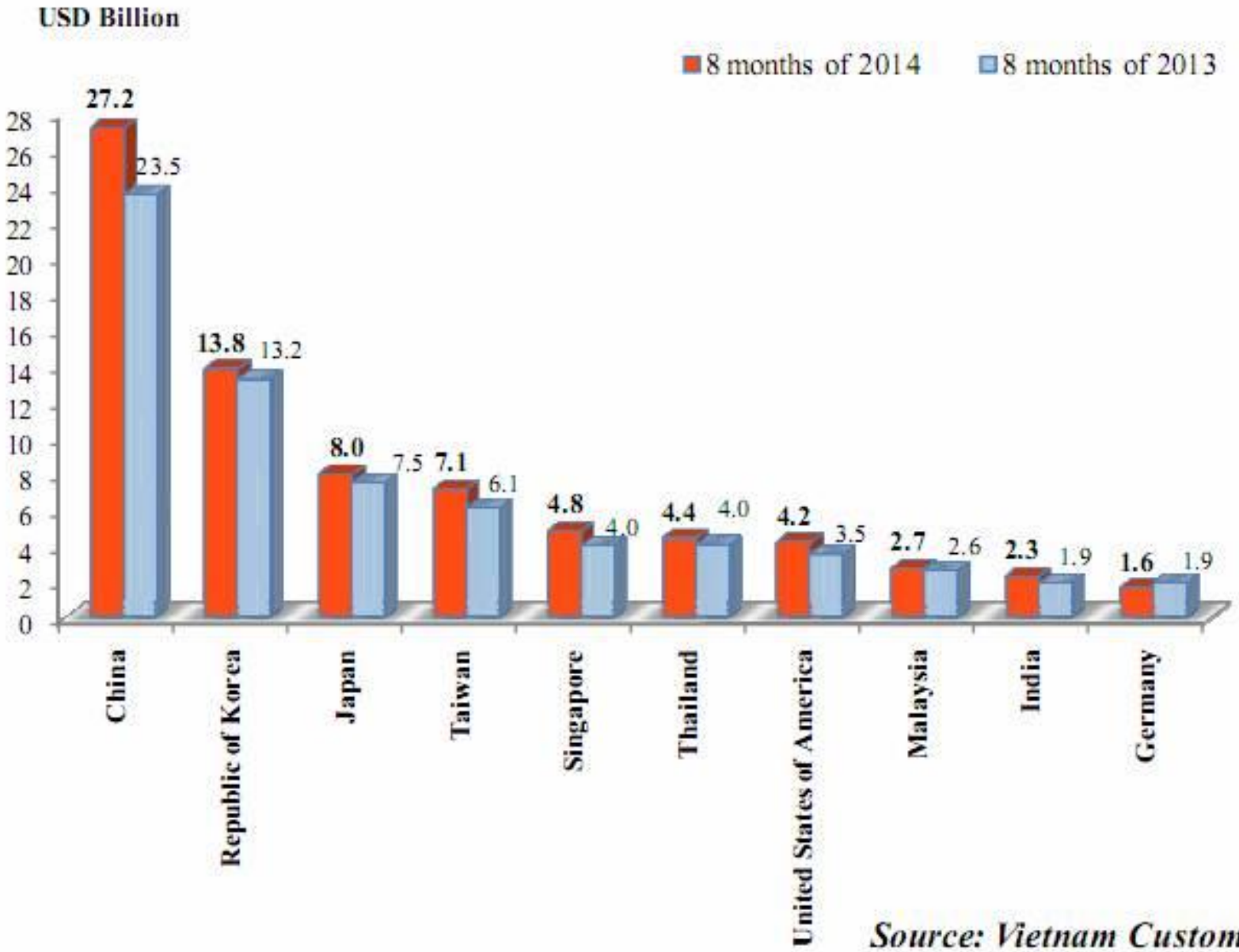
Chart 2: Top 10 main importing markets of Vietnam in the 8 months of 2014



Source: Vietnam Customs

Table 1: OVERVIEW OF VIETNAM INTERNATIONAL MERCHANDISE TRADE STATISTICS IN AUGUST AND THE 8 MONTHS OF 2014

No.		Main Trade Indicators (in nominal terms and not seasonally adjusted)	
(A)		(B)	(C)
I		**Merchandise Export (EX)**	
1	I.1	Total value of August, 2014 (Million US$)	13,272
2	I.2	Change as compared with July, 2014 (%)	2.8
3	I.3	Change as compared with August, 2013(%)	12.6
4	I.4	Total value of the 8 months of 2014 (Mil. US$)	97,233
5	I.5	Change as compared with the 8 months of 2013 (%)	14.4
II		**Merchandise Import (IM)**	
6	II.1	Total value of August, 2014 (Mil. US$)	12,198
7	II.2	Change as compared with July, 2014 (%)	-5.9
8	II.3	Change as compared with August, 2013 (%)	8.1
9	II.4	Total value of the 8 months of 2014 (Mil. US$)	94,162
10	II.5	Change as compared with the 8 months of 2013 (%)	10.7
III		**Total Merchandise Trade Value (EX+IM)**	
11	III.1	Total trade value of August, 2014 (Mil. US$)	25,470
12	III.2	Change as compared with July, 2014 (%)	-1.6
13	III.3	Change as compared with August, 2013 (%)	10.4
14	III.4	Total trade value of the 8 months of 2014 (Mil. US$)	191,395
15	III.5	Change as compared with the 8 months of 2013 (%)	12.5
IV		**Merchandise Trade Balance (EX-IM)**	
16	IV.1	Trade balance of August, 2014 (Mil. US$)	1,074
17	IV.2	Trade balance of the 8 months of 2013 (Mil. US$)	3,071

Source: Vietnam Customs

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Table 2: Top 10 major exported commodities of Vietnam in August, 2014

No	Main exports	August (USD million)	Compared with previous month (%)	Year to date (USD million)	Compared with previous year (%)
1	Textiles and garments	2,144	-0.1	13,607	19.4
2	Telephones, mobile phones and parts thereof	1,844	3.5	15,185	13.4
3	Computers, electrical products, spare-parts and components thereof	989	7.0	6,509	-3.6
4	Foot-wears	914	-3.3	6,688	22.9
5	Fishery products	763	5.6	5,034	25.1
6	Crude oil	698	-4.6	5,339	9.2
7	Machine, equipment, tools and instruments	649	2.1	4,717	21.9
8	Wood and wooden products	554	12.0	3,944	14.9
9	Other means of transportation, parts and accessories thereof	439	-0.5	3,761	8.9
10	Rice	302	11.3	2,041	-3.9

Source: Vietnam Customs

Table 3: Top 10 major imported commodities of Vietnam in August, 2014

No	Main imports	August (USD million)	Compared with previous month (%)	Year to date (USD million)	Compared with previous year (%)
1	Machine, equipment, tools and instruments	1,967	-8.1	14,193	21.2
2	Computers, electrical products, spare-parts and components thereof	1,465	2.1	11,158	-3.0
3	Textile, leather and foot- wears materials and auxiliaries group	1,303	-13.6	11,197	16.7
4	Telephones, mobile phones and parts thereof	699	21.9	5,203	0.4
5	Iron and steel	687	-4.2	4,736	5.4
6	Plastics	550	-3.6	4,119	12.3
7	Petroleum products	526	-37.9	5,725	22.3
8	Chemicals	289	-8.1	2,148	8.3
9	Animal fodders and animal fodders materials	286	-5.5	2,206	6.7
10	Chemical products	280	-7.8	2,091	16.9

Source: Vietnam Customs

Who Trades with Whom?

- The 5 largest trading partners with Vietnam: China, EU, USA, South Korea, Japan
- The total value of imports from and exports to Vietnam in 2014 was about $298.24 billion dollars (12.9% increase compared to 2013)
  - Exports 2014 reached $150.19 billion
  - Imports 2014 reached $148.05 billion
  - Trade surplus $2.14 billion (highest so far and 3rd year surplus in a row)

Source: Vietnam Customs as of 23/01/2015

http://customs.gov.vn/Lists/ThongKeHaiQuan/ViewDetails.aspx?ID=792&Category=Tin%20v%E1%BA%AFn%20th%E1%BB%91ng%20k%C3%AA&Group=Ph%C3%A2n%20t%C3%ADch

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Law of Gravity

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The Gravity Model

- 3 of the top 6 trading partners with Vietnam in 2014 are Asian economies: China, Japan, and South Korea.
- Why does China top list of Vietnam's trade partners?
- How does gravity model apply to ASEAN countries?
- How does gravity model apply to Trans-Pacific Partnership (TPP) participating countries?

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The Gravity Model (cont.)

- In fact, the size of an economy is directly related to the volume of imports and exports.
  - Larger economies produce more goods and services, so they have more to sell in the export market.
  - Larger economies generate more income from the goods and services sold, so they are able to buy more imports.

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The Gravity Model

Other things besides size matter for trade:

1. *Distance* between markets influences transportation costs and therefore the cost of imports and exports.
   - Distance may also influence personal contact and communication, which may influence trade.
2. *Cultural affinity*: if two countries have cultural ties, it is likely that they also have strong economic ties.
3. *Geography*: ocean harbors and a lack of mountain barriers make transportation and trade easier.

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The Gravity Model (cont.)

4. *Multinational corporations*: corporations spread across different nations import and export many goods between their divisions.

5. *Borders*: crossing borders involves formalities that take time and perhaps monetary costs like tariffs.
   - These implicit and explicit costs reduce trade.
   - The existence of borders may also indicate the existence of different languages (see 2) or different currencies, either of which may impede trade more.

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The Gravity Model (cont.)

- In its basic form, the gravity model assumes that only size and distance are important for trade in the following way:

$$T_{ij} = A \times Y_i \times Y_j / D_{ij}$$

- where

  T_{ij} is the value of trade between country *i* and country *j*

  A is a constant

  Y_i the GDP of country *i*

  Y_j is the GDP of country *j*

  D_{ij} is the distance between country *i* and country *j*

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The Gravity Model (cont.)

- In a slightly more general form, the gravity model that is commonly estimated is

$$T_{ij} = A \times Y_i^a \times Y_j^b / D_{ij}^c$$

where *a, b,* and *c* are allowed to differ from 1.

- Despite its simplicity, the gravity model works fairly well in predicting actual trade flows, as the figure above representing U.S.–EU trade flows suggested.

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Distance and Borders

- Estimates of the effect of distance from the gravity model predict that a 1% increase in the distance between countries is associated with a decrease in the volume of trade of 0.7% to 1%.

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Distance and Borders (cont.)

- Besides distance, borders increase the cost and time needed to trade.
- *Trade agreements* between countries are intended to reduce the formalities and tariffs needed to cross borders, and therefore to increase trade.
- The gravity model can assess the effect of trade agreements on trade: does a trade agreement lead to significantly more trade among its partners than one would otherwise predict given their GDPs and distances from one another?

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Has the World Become "Smaller"?

- The negative effect of distance on trade according to the gravity models is significant, but has grown smaller over time due to modern transportation and communication.
- Technologies that have increased trade:
  - Wheels, sails, compasses, railroads, telegraph, steam power, automobiles, telephones, airplanes, computers, fax machines, Internet, fiber optics, personal digital assistants, GPS satellites…

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Has the World Become "Smaller"? (cont.)

- Political factors, such as wars, can change trade patterns much more than innovations in transportation and communication.
- World trade grew rapidly from 1870 to 1913.
  - Then it suffered a sharp decline due to the two world wars and the Great Depression.
  - It started to recover around 1945 but did not recover fully until around 1970.
- Since 1970, world trade as a fraction of world GDP has achieved unprecedented heights.

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Table 2-2: World Exports as a Percentage of World GDP

TABLE 2-2	World Exports as a Percentage of World GDP
1870	4.6
1913	7.9
1950	5.5
1973	10.5
1998	17.2

Source: Angus Maddison, *The World Economy: A Millennial Perspective*, World Bank, 2001.

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Changing Composition of Trade

- What kinds of products do nations trade now, and how does this composition compare to trade in the past?
- Today, most (about 55%) of the volume of trade is in *manufactured products* such as automobiles, computers, clothing and machinery.
  - *Services* such as shipping, insurance, legal fees, and spending by tourists account for about 20% of the volume of trade.
  - *Mineral products* (ex., petroleum, coal, copper) and *agricultural products* are a relatively small part of trade.

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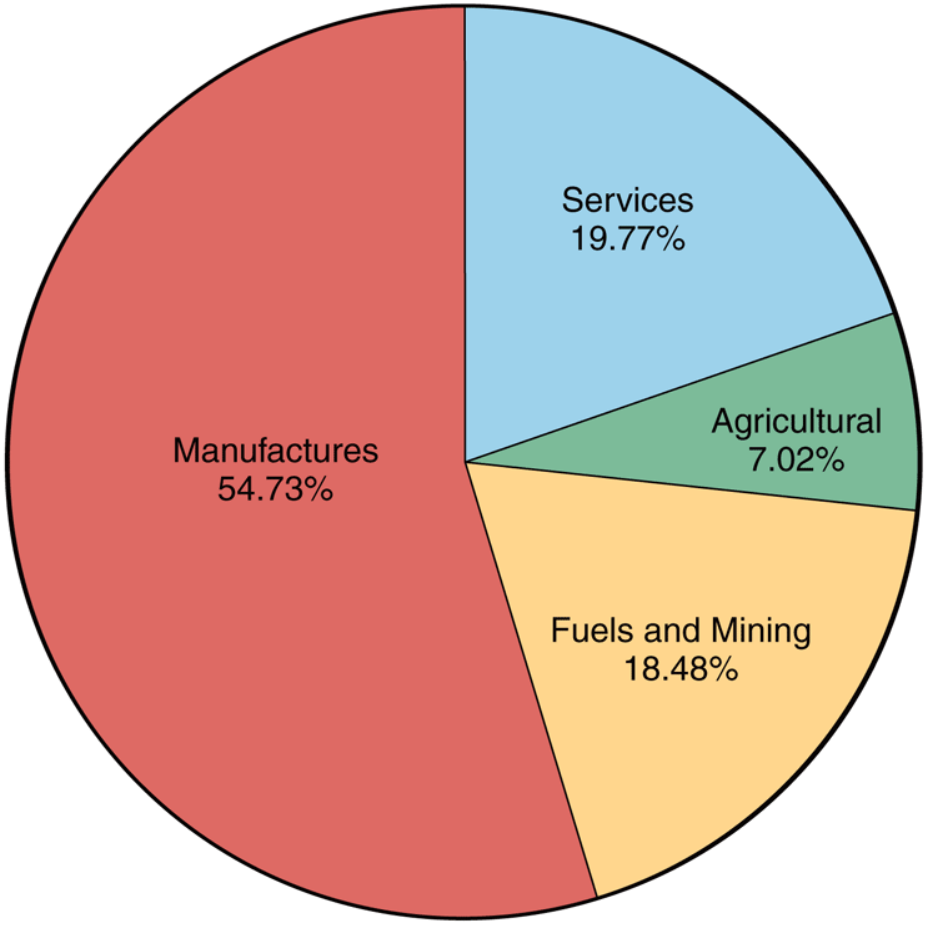
Fig. 2-5: The Composition of World Trade, 2008



Source: World Trade Organization

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Changing Composition of Trade (cont.)

- In the past, a large fraction of the volume of trade came from agricultural and mineral products.
  - In 1910, Britain mainly imported agricultural and mineral products, although manufactured products still represented most of the volume of exports.
  - In 1910, the U.S. mainly imported and exported agricultural products and mineral products.
  - In 2002, manufactured products made up most of the volume of imports and exports for both countries.

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Table 2-3: Manufactured Goods as a Percent of Merchandise Trade

TABLE 2-3 Manufactured Goods as Percent of Merchandise Trade

	United Kingdom		United States	
	Exports	Imports	Exports	Imports
1910	75.4	24.5	47.5	40.7
2008	71.0	67.8	74.8	65.3

Source: 1910 data from Simon Kuznets, *Modern Economic Growth: Rate, Structure and Speed.* New Haven: Yale Univ. Press, 1966. 2008 data from World Trade Organization.

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Changing Composition of Trade (cont.)

- Low- and middle-income countries have also changed the composition of their trade.
  - In 2001, about 65% of exports from low- and middle-income countries were manufactured products, and only 10% of exports were agricultural products.
  - In 1960, about 58% of exports from low- and middle-income countries were agricultural products and only 12% of exports were manufactured products.

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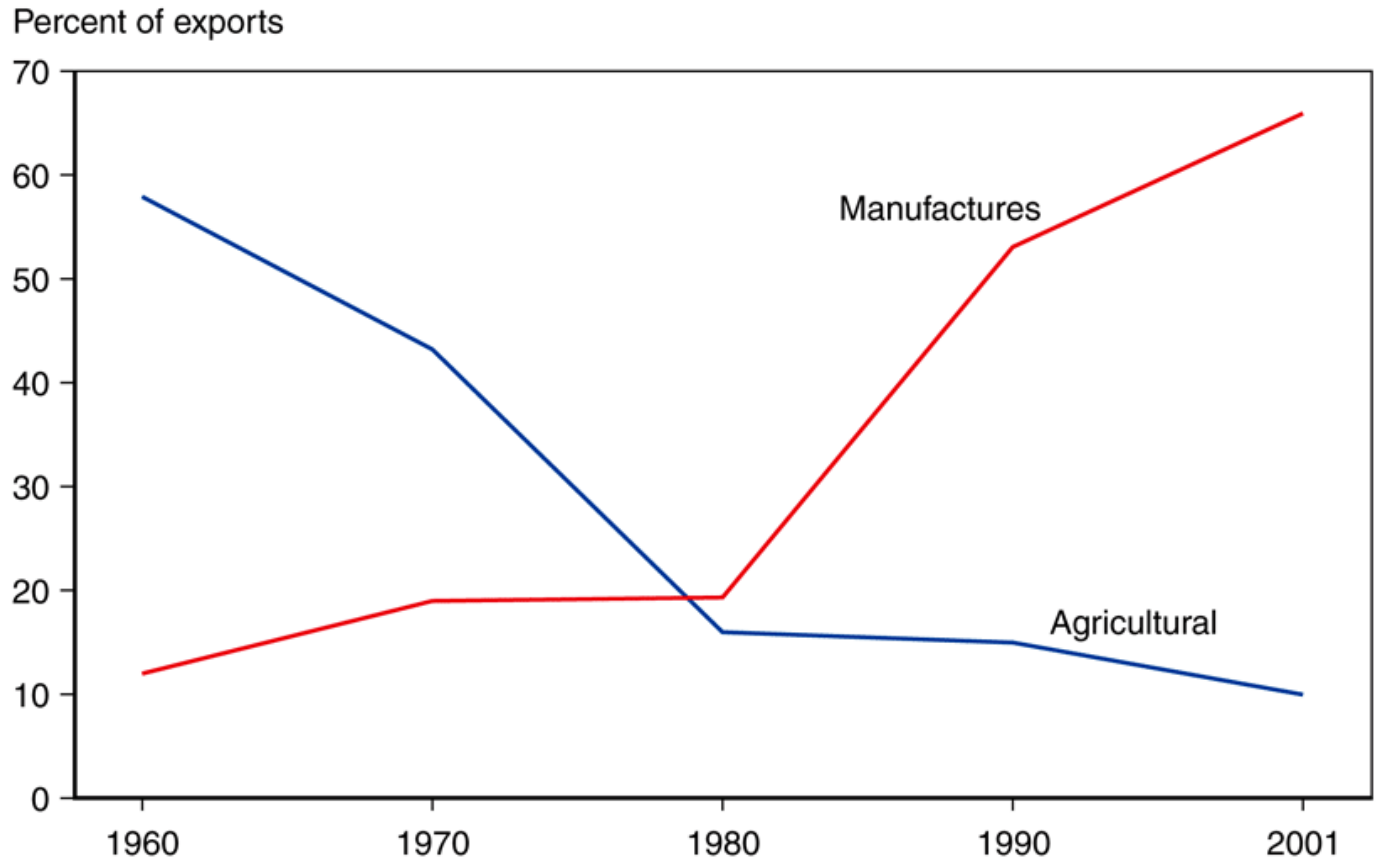
Fig. 2-6: The Changing Composition of Developing-Country Exports



Source: United Nations Council on Trade and Development

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Service Outsourcing

- **Service outsourcing (or offshoring)** occurs when a firm that provides services moves its operations to a foreign location.
  - Service outsourcing can occur for services that can be performed and transmitted electronically.
    - For example, a firm may move its customer service centers whose telephone calls can be transmitted electronically to a foreign location.

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Service Outsourcing (cont.)

- Service outsourcing is currently not a significant part of trade.
  - Some jobs are "tradable" and thus have the potential to be outsourced.
  - Most jobs are nontradable because they need to be done close to the customer.

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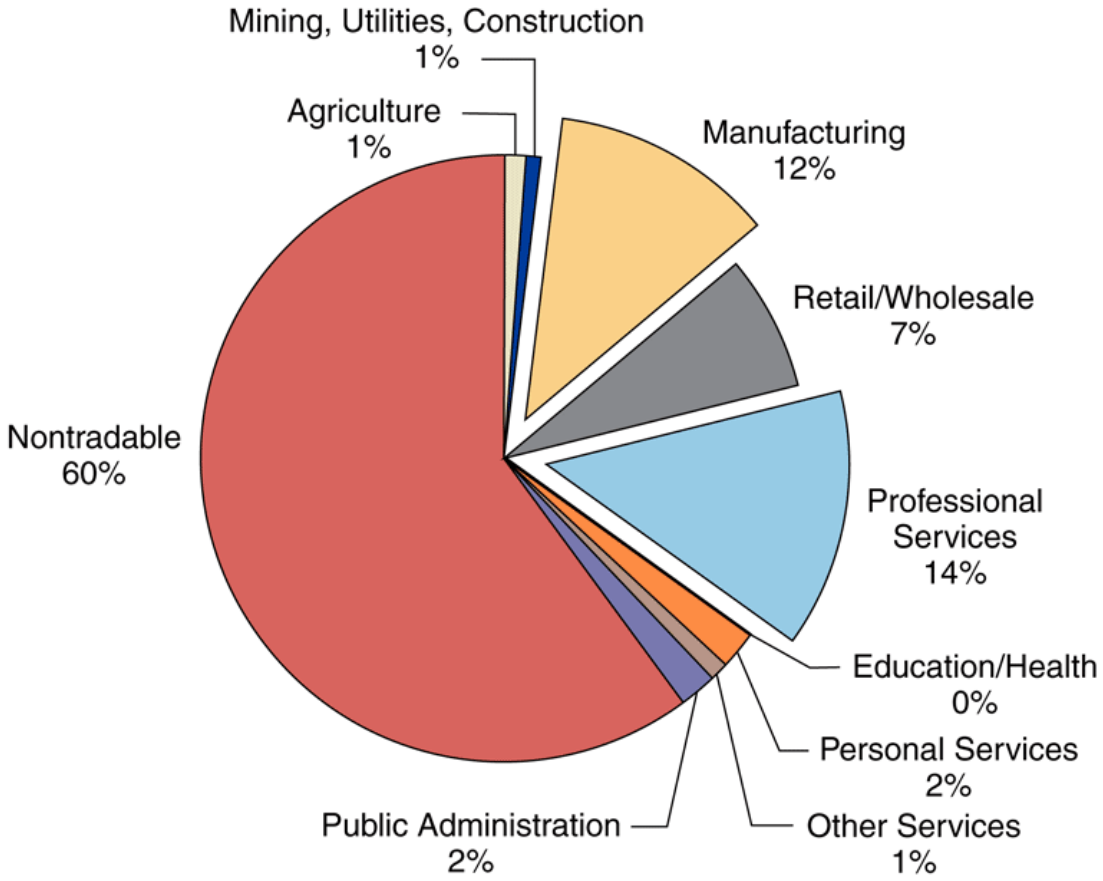
Fig. 2-7: Tradable Industries' Share of Employment



Source: J. Bradford Jensen and Lori G. Kletzer, "Tradable Services: Understanding the Scope and Impact of Services Outsourcing," Peterson Institute of Economics Working Paper 5-09, May 2005

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Summary

1. The largest trading partners with Vietnam
2. The gravity model predicts that the volume of trade is directly related to the GDP of each trading partner and is inversely related to the distance between them.
3. Besides size and distance, culture, geography, multinational corporations, and the existence of borders influence trade.
4. Modern transportation and communication have increased trade, but political factors have influenced trade more in history.
5. Today, most trade is in manufactured goods, while historically agricultural and mineral products made up most of trade.

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