Department for
International Trade

Impact assessment of the EU-Vietnam Free Trade Agreement (EVFTA) on the UK

29/03/2019

Title: Impact assessment of the EU-Vietnam Free Trade Agreement (EVFTA) on the UK **IA No: DIT0009** **RPC Reference No:** RPC-4328(1)-DIT **Lead department or agency:** Department for International Trade **Other departments or agencies:** N/A	**Impact Assessment (IA)** **Date: 07/03/2019** **Stage: Final** **Source of intervention: EU** **Type of measure: Other** **Contact for enquiries:** enquiries@trade.gov.uk

Summary: Intervention and Options

RPC Opinion: Green

Cost of Preferred (or more likely) Option				
Total Net Present Value	**Business Net Present Value**	**Net cost to business per year** (EANDCB in 2014 prices)	**One-In, Three-Out**	**Business Impact Target Status**
£5,100 m	N/A	N/A	No	Not a regulatory provision

What is the problem under consideration? Why is government intervention necessary?

The European Commission and the Government of Vietnam have concluded negotiations and agreed a final text for the EU-Vietnam Free Trade Agreement (EVFTA). The European Commission has presented a proposal on signature and conclusion of this agreement to the Council of the European Union, which now has to decide whether to formally adopt the necessary Council Decision authorising signature of the Agreement. In the past, Council Decisions on signature of EU trade agreements have typically been agreed through Common Accord, requiring the agreement of all Member States. UK parliament will be required to vote for or against the signature and conclusion of the EVFTA. The position the UK will take on this will be subject to UK Parliamentary scrutiny. Upon signature, the EVFTA will require European Parliament approval and ratification by Vietnam before it can enter into force.

What are the policy objectives and the intended effects?

The policy objectives are to support the EU's free trade agenda whilst we are still an EU member state, specifically the implementation of EVFTA. The intended effects are increased bilateral trade and economic growth, and support for Vietnam's economic and social transformation and integration into the global economy. The Agreement includes elimination of most tariffs between the EU and Vietnam and addresses non-tariff barriers including public procurement rules, regulatory issues, competition, services, investment, intellectual property rights, and sustainable development. The EVFTA will lower costs of UK exports and imports and give more opportunity for UK businesses in Vietnam. Furthermore, EVFTA will increase the welfare of UK households by lowering the price of goods. Baker and Vanzetti (2019) shows that the EVFTA could increase UK exports to Vietnam by 60% (equivalent to around £490 million) per annum in the long run. In addition, UK consumer welfare is expected to increase by £290 million from an increase in real income. Overall UK GDP is estimated to increase by 0.01% which equates to around £390 million per annum in the long run.

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)

EU and Vietnam have concluded EVFTA negotiations and so there is no scope to change its content at this stage. The policy options are therefore to support, or not, signature of the agreement. The options, assessed against a baseline of no agreement, are:

1. **The UK votes in favour of signature** and conclusion of the EVFTA. Providing the other EU Member States also vote in favour, the effect would be the EVFTA signed and entering into force once the European Parliament has given its consent and Vietnam has completed its ratification procedure. **This is the Government's preferred option.**
2. **The UK does not support signature** and conclusion of the Agreement. In this case, the means by which Council voted could have a bearing on the outcome. If Council approval were sought via Common Accord, the UK failing to vote in favour would prevent the agreement from being signed and concluded. Dialogue to try to unblock signature would be likely, but the practical impact would be the EU and Vietnam continuing to trade on WTO Most Favoured Nation terms and the UK not accruing any additional benefits above the baseline of this IA. Alternatively, Council approval might be sought via Qualified Majority Vote, with potential for the agreement to be signed if a sufficient number of Member States vote in favour, even without UK support.

Will the policy be reviewed? No. **If applicable, set review date: N/A**

Does implementation go beyond minimum EU requirements?	No			
Are any of these organisations in scope?	**Micro** Yes	**Small** Yes	**Medium** Yes	**Large** Yes
What is the CO_2 equivalent change in greenhouse gas emissions? (Million tonnes CO_2 equivalent)	**Traded:** N/Q		**Non-traded:** N/Q	

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible SELECT SIGNATORY: George Hollingbery Date: 27th March 2019

Summary: Analysis & Evidence — Policy Option 1

Description: The UK votes in favour of signature of the EU-Vietnam FTA. This is the government's preferred option and the one being taken forward. FULL ECONOMIC ASSESSMENT

Price Base Year 2017	PV Base Year 2017	Time Period Years 15	Net Benefit (Present Value (PV)) (£m)		
			Low: -	**High: -**	**Best Estimate: 5,100**

COSTS (£m)	**Total Transition** (Constant Price)		**Average Annual** (excl. Transition) (Constant Price)	**Total Cost** (Present Value)
Low	1.4		-	1.4
High	1.3		-	**1.3**
Best Estimate	1.4		-	**1.3**

Description and scale of key monetised costs by 'main affected groups'

UK businesses are not expected to incur costs if they do not utilise the preferences set out in the EVFTA.
Where a business chooses to trade under the EVFTA they will incur a one-off familiarisation cost associated with reading the free trade agreement guidance (£1.4 million).

Other key non-monetised costs by 'main affected groups'

There will be lower domestic production in some sectors due to increased competition from imports. This is captured within the net GDP effects set out below.

BENEFITS (£m)	**Total Transition** (Constant Price)		**Average Annual** (excl. Transition) (Constant Price)	**Total Benefit** (Present Value)
Low	-		-	**-**
High	-		-	**-**
Best Estimate	-		420	**5,100**

Description and scale of key monetised benefits by 'main affected groups'

Figures presented here reflect the long run impacts per annum and should be treated as a magnitude of change and not a forecast.

Baker and Vanzetti (2019) estimate the long run net increase in UK real Gross Domestic Product (GDP) to be around 0.01% per annum in the long run (equivalent to around £390 million). These benefits include the elimination of most tariffs and the reduction of actionable Non-Tariff Measures (NTM) that impede cross-border trade in goods and services. The impact assessment is based on the results of external Computable General Equilibrium (CGE) modelling undertaken by Baker and Vanzetti (2019) which is sensitive to the assumptions and methodologies applied. The results are not a forecast and should be treated as indicative of the plausible magnitude and direction of impacts, rather than precise predictions. The estimates in Baker and Vanzetti (2019) are based on the authors' interpretation of the EVFTA text and their judgement on the additional market access offered under the agreement. The results are therefore subject to a degree of uncertainty.

The increase in net GDP is associated with:

- An increase in UK **bilateral exports** by 60% which equates to around £490 million per annum.
- An increase in UK **bilateral imports** by 33%, which equates to around £1.7 billion per annum.

Alongside these benefits the estimates suggest a £290 million increase in UK consumer welfare from an increase in real income.
Most of the UK bilateral export gains will be trade in service sectors. UK import gains are expected to be in textiles, leather and motor vehicle parts. These are economic changes that underlie and drive the change in GDP, but they are not additive components of GDP.

Other key non-monetised benefits by 'main affected groups'

Increase in consumer choice of goods and services.
Efficiency savings from a reduction in some non-tariff measures (NTMs), for example, the mutual recognition of conformity assessment bodies.
UK business will benefit from greater ease to bid for Vietnamese government contracts.

Key assumptions/sensitivities/risks — **Discount rate (%)** 3.5%

- The analysis assumes that the Government is able to deliver its stated policy intention to ensure continuity in the effect of EU agreements as the UK leaves the EU, and therefore ensures broadly similar trade preferences in the long run between the UK and Vietnam. Whilst the UK-EU access to each other's markets may, in certain ways, be less than it is now, it is not currently possible to model how that would change the baseline.
- The analysis assumes this agreement will be continued bilaterally with Vietnam once the UK leaves the EU without changes to rules of origin.
- Estimates are produced against a 2018 baseline which includes the tariff eliminations associated with the Comprehensive & Progressive Trans-Pacific Partnership agreement (CPTPP) and trade agreements the EU has recently concluded such as the EU-Canada Comprehensive and Economic Partnership Agreement (CETA) and the EU-Singapore FTA.

BUSINESS ASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £m			**Score for Business Impact Target (qualifying provisions only) £m: Not a regulatory provision**
Total Costs: N/A	**Total Benefits: N/A**	**Net: N/A**	

Evidence Base

The structure of this Impact Assessment is as follows:

1: Economic background
2: Strategic overview of EVFTA
3: Problem under consideration
4: Rationale for intervention
5: Policy objective
6: Description of options considered
7: Monetised and non-monetised costs and benefits of each option
8: Small and Micro Business Assessment
9: Direct costs and benefits to business calculations
10: Sensitivities
11: Risks and assumptions

1 Economic background

1.1 Under the UK's current membership of the EU, decisions on trade policy are taken by the Council of the European Union and the European Parliament. The day to day conduct of EU trade relations, including the negotiation of free trade agreements, is led by the European Commission.

1.2 While we are members of the EU, we will continue to cooperate fully and constructively with our partners fulfilling the responsibilities of a Member State. Once we have left, we will work collaboratively with the EU to press our shared free trade agenda. We will then also have the opportunity to advance our interests, priorities and ambitions through a new independent trade policy.

The world in which the UK trades

1.3 Free and fair trade is fundamental to the prosperity of the EU and the world economy. Trade has historically been an important part of the UK economy. Excluding major shocks such as the Great Depression and two World Wars, both exports and imports have accounted for over 20% of UK GDP for the last 160 years.[1]

1.4 A substantial proportion of the growth in global trade in recent decades has been driven by growth in intra-industry trade and the development of cross-border supply chains, where different stages of production for a particular good are located in different countries. Well-functioning global trade relationships help businesses to manage their supply chains effectively and source the imports they need for their business. Over 70% of global trade is now in intermediate products, or in capital goods (many of which are employed in the production of other goods).[2] Intra-industry trade (the import and export of the same or similar goods) has increased; in the late 1980s, 70% of UK manufacturing trade was intra-industry, whereas between 1997 and 2008, intra-industry trade increased to over 80%.[3]

1.5 This has driven significant shifts in shares of world trade. Developed economies' share of global exports fell from 69% in 1980 to 54% in 2013.[4]

1.6 Services are also an important, and growing, component of supply chains. Firms increasingly use logistics, communications services, and business services to enable the efficient functioning of their supply chains, and almost one third of the value of manufactured exports of developed countries comes from service intermediate inputs.[5] Digital technology is continuing to rapidly develop, facilitating economic growth and making more and more services tradable.[6]

1.7 Trade agreements at the multilateral, plurilateral and bilateral level help to facilitate international trade.

[1] DIT using Bank of England research datasets: Three centuries of macroeconomic data. see http://www.bankofengland.co.uk/research/Pages/datasets/default.aspx
[2] OECD, see for example https://www.oecd.org/tad/gvc_report_g20_july_2014.pdf
[3] Economic Globalisation Indicators', (2012) and OECD, 'Intra Industry and Intra Firm Trade and the Internationalisation of Production', Economic Outlook, (2002)
[4] DIT estimates based on UNCTAD trade data.
[5] WTO working paper see https://www.wto.org/english/res_e/reser_e/ersd201503_e.pdf
[6] https://www.gov.uk/ukdigitalstrategy.

The benefits of international trade

Global benefits

1.8 An open and rules-based international trading environment enables economic integration and security cooperation. It encourages predictable behaviour by states and the peaceful settlement of disputes. It can also lead states to develop political and economic arrangements at home which favour open markets, the rule of law, participation and accountability.

Growth, prosperity and jobs

1.9 Empirical studies generally suggest a positive relationship between trade openness and economic growth. The dramatic increase in China's growth since it opened up its economy provides a striking example, and analysis by the OECD suggests that a 10% increase in openness is associated with a 4% increase in income per head.[7]

1.10 Trade enables countries, firms and individuals to specialise in economic activities that play to their relative strengths, resources and expertise, and to buy from and sell to other countries doing likewise. Specialisation increases global output and increases the quality and value of goods and services for consumers.

1.11 Free trade also allows businesses to benefit from access and exposure to ideas, talent and technology across borders, and so become more competitive. Businesses that export into new markets can access more customers and help grow overall UK exports which contribute to growth in the UK economy.

Choice, value and quality for consumers

1.12 Free trade and imports improve living standards for consumers, through the variety and price of goods available.

1.13 Consumers and households benefit directly through lower tariffs on imported final consumption goods. They also benefit indirectly as firms become more productive. For example, during 1996 – 2006 import prices for textiles and clothing fell by 27% and 38% respectively in real terms, in large part because of the phasing out of restrictive quotas in developed countries. For the same period the import price of consumer electronics fell by around 50%,[8] reflecting the impact of the Information Technology Agreement.

[7] OECD (2003), Sources of Economic Growth in OECD Countries, 'https://www.oecd.org/eco/growth/2505752.pdf

[8] J. Francois, M. Manchin, and H. Norberg, 2007, "Passing on of the benefits of trade openness to consumers", European Commission, Directorate General for Trade, p.7.

1.14 Free trade drives businesses to innovate and move up the value chain to compete with cheaper imports to set themselves apart which means that consumers benefit from better quality and ever improving products, at lower prices.

Summary

1.15 Countries engage in trade because it is mutually beneficial and can benefit businesses, consumers and the wider economy. Businesses gain from greater revenue and profit which can lead to more investment, productivity and innovation. Consumers gain from greater choice in the variety and quality of goods and services, lower prices through increased competition, higher real wages and living standards. Trade allows countries to allocate their resources to activities in which they are more productive.

1.16 Domestic government policies may reduce trade flows between countries and the associated benefits. The most obvious policy measures are tariffs, subsidies and quantitative restrictions, but barriers also include complex regulations (for example, health and safety, packaging, labelling and product regulations) and customs procedures. These restrict free trade, which distorts the market price, lowering competition and reducing choice for consumers.

1.17 Given the benefits of free trade, liberalisation generally has a positive impact on GDP and citizens' welfare. However, changes in the pattern of trade do lead to some sectors expanding and some sectors declining in response to increased international competition.

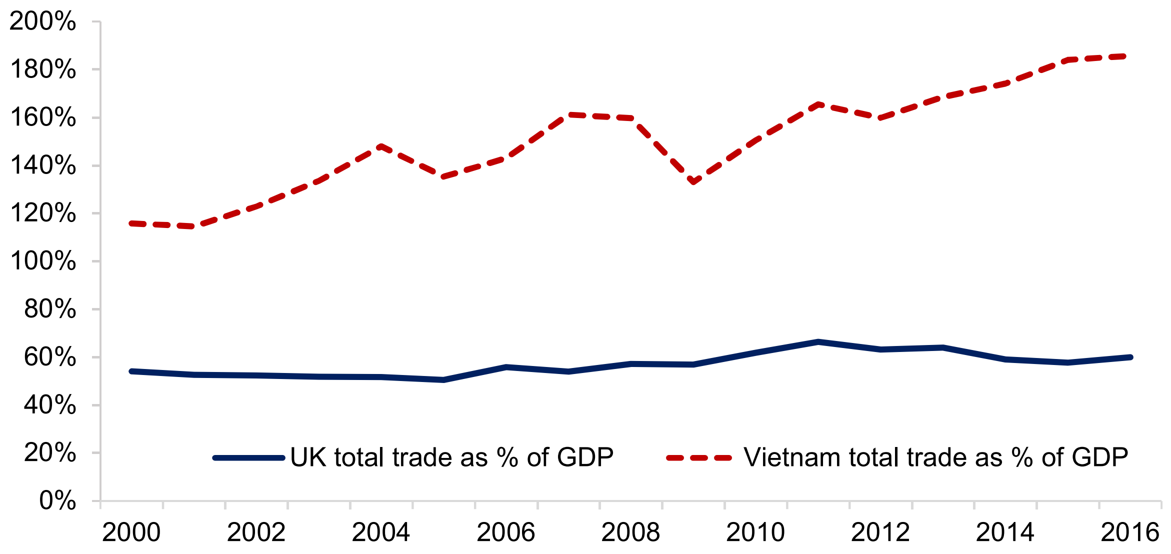
Trade between the UK and Vietnam

1.18 This section examines current trade flows between the UK and Vietnam and the extent to which trade is restricted by tariffs and non-tariff measures (NTMs).

1.19 In 2017, Vietnam had GDP per capita equal to £1,800. This figure is lower than the UK's which is equal to £30,000. However per capita income in Vietnam has grown at an average of 11% since 2000[9]. This strong growth can, in part, be explained by Vietnam's increasing openness to international markets. Graph 1, below, shows that the value of total trade in Vietnam as a percentage of GDP has been steadily climbing since 2000.

1.20 Over this period there have been important shifts in the structure of Vietnam's exports of commodities to the UK and wider EU. Previously, Vietnamese products mainly comprised agri-food, footwear, and apparel, many of which were in the form of raw materials or simple processing with little value added. Nowadays, with strong presence from overseas firms that have invested in the country, Vietnam exports more sophisticated products. For example, Samsung, a Korean smartphone manufacturer, has provided multi-billion pound investment into Vietnam which has transformed Vietnam into a regional hub for assembling smartphones, with around one third being exported to Europe.

Graph 1: Total trade as a percentage of GDP



Source: UN Comtrade for total trade data (https://comtrade.un.org/) and World Bank for GDP data (https://data.worldbank.org/)

[9] Nominal GDP per capita, World Bank data: https://data.worldbank.org/

1.21 Strong growth in both Vietnam's GDP and trade is forecast to continue[10]. Graph 1 shows Vietnam's total trade as a share of its GDP has increased from 2000 to 2016 whereas the UK's total trade as a share of its GDP has remained relatively constant. Estimates suggest GDP growth will average at 5% until 2050,[11] driven by Vietnam's cost competitive production base and a young digitally-savvy workforce.[12] As of 2017, 40% of Vietnam's 96 million population is under the age of 25.[13] Given this positive outlook the EVFTA should help increase the £4.7 billion of goods and services the UK already trades with Vietnam.

1.22 As Vietnam's middle class grows and disposable incomes rise, greater spending power is generating demand for services and higher value-added products.[14] This provides opportunities for increased services trade between the UK and Vietnam given the UK's service based economy.

1.23 In 2016 the UK exported just under £800 million worth of goods and services to Vietnam. In comparison, the UK imported around £4,000 million worth of goods and services from Vietnam resulting in a UK trade deficit with Vietnam.

1.24 As seen in graph 2, the UK imports more goods from Vietnam than it exports. In 2017 the UK imported £4.2 billion worth of goods from Vietnam including electrical machinery, footwear and apparel. The large increases in more recent years reflect two factors: firstly, Vietnam has become better integrated into the global trade network since its accession to the WTO in 2007. Secondly, as Vietnam's economy transitions through the development phases demand for low-cost electrical machinery has increased throughout Europe and the USA.

1.25 Graph 2 also highlights limited trade in services between the two nations. One of the reasons for this is that Vietnam has not yet developed a services sector from which it can compete on a global stage and thus export from. In 2017, services sector accounted for more than 40% of Vietnam's GDP, which was still low in comparison with that of developed countries (around 80% in the UK for example). However, Vietnam's economy is developing and the demand for high-quality financial, legal and other professional services is increasing. With the opening of the UK and Vietnam markets as a result of the EVFTA, it is expected that bilateral trade in services will be boosted in the future, particularly for the UK in the short and medium term.

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10 PwC (2017). 'The World in 2050'. https://www.pwc.com/gx/en/issues/economy/the-world-in-2050.html

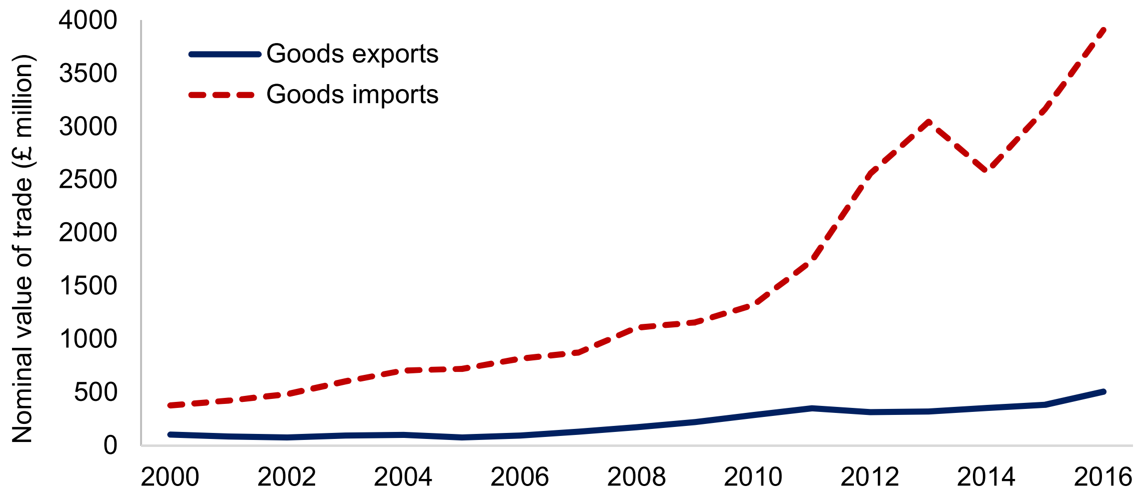
11 Source: PwC (2017) 'Doing Business in Vietnam' https://www.pwc.com/vn/en/publications/2017/dbg-2017.pdf. Data based on International Monetary Fund (IMF) analysis. To note, the analysis presented in section 7 assumes Vietnams economy growths by 5.6% in 2015 down to 3.8% in 2020 and levels off at 4.3% in 2030. See section 11 for more information.

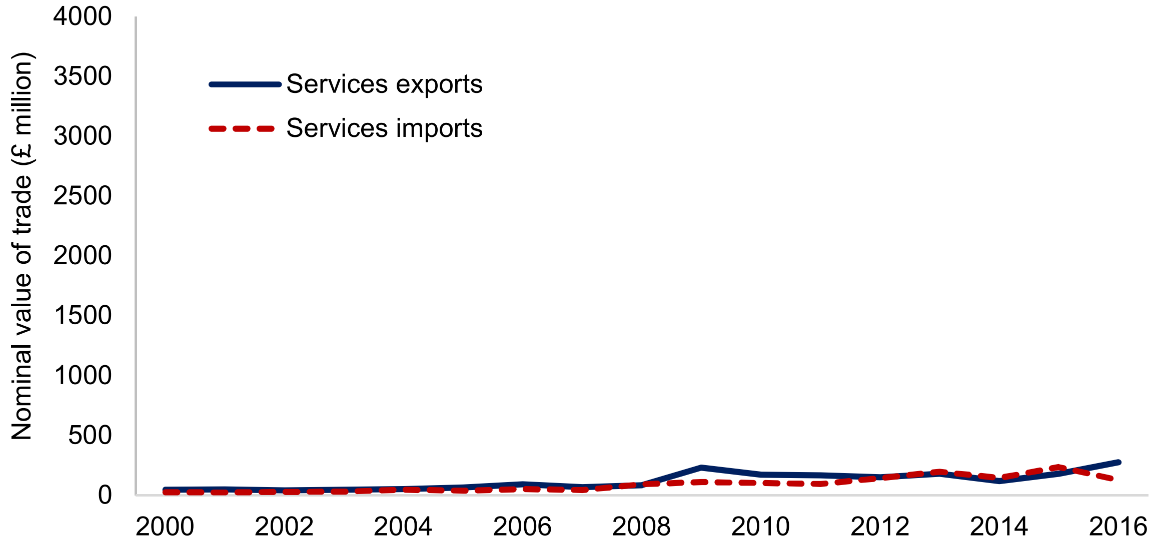
12 PwC (2017). 'Doing Business in Viet Nam'. https://www.pwc.com/vn/en/publications/2017/dbg-2017.pdf

13 Source: World Bank Data. https://data.worldbank.org/indicator/SP.POP.TOTL?locations=VN.

14 PwC Vietnam (2018). 'The Future of ASEAN: Viet Nam Perspective' https://www.pwc.com/vn/en/publications/2018/pwc-vietnam-future-of-asean-vietnam-perspective.pdf

Graph 2: UK trade in goods and services with Vietnam





Source: Office for National Statistics, Pink Book 2017 (https://www.ons.gov.uk/releases/unitedkingdombalanceofpaymentsthepinkbook2017)

1.26 The top 10 goods exported and imported between the UK and Vietnam can be seen in Table 1. These accounted for 71% and 87% of the total goods exported to and imported from the UK to Vietnam respectively. Between 2015 and 2017 the UK mostly exported machinery and mechanical appliance to Vietnam, followed by pharmaceutical products and electrical machinery. By far the top UK import from Vietnam is electrical machinery, representing 40% of all goods imports from Vietnam. Breaking down this category further, around £1.37 billion of the £1.47 billion is in smartphones. For comparison, in 2010, UK imports of electrical machinery from Vietnam were only £68 million, with footwear and apparel the largest imports. This is evidence again of the rapid development Vietnam is undergoing as it shifts from lower to higher skilled manufacturing.

Table 1: Top 10 UK goods exports and imports on average 2015 to 2017

Product Categories	3 year average value (£, millions)	Proportion of total exports/imports to/from Vietnam
Top 10 goods exports to Vietnam		
Machinery and mechanical appliances	107	22%
Pharmaceutical products	56	12%
Electrical machinery	45	9%
Optical, photographic, cinema	29	6%
Plastics and plastic products	23	5%
Vehicles other than railway	21	4%
Fish and crustaceans	18	4%
Miscellaneous chemical products	17	4%
Residues and waste from the food industries	13	3%
Pulp of wood or of other fibrous cellulosic material	13	3%
Top 10 goods imports from Vietnam		
Electrical machinery	1,470	40%
Footwear	454	12%
Articles of apparel (not knitted)	323	9%
Furniture	277	8%
Machinery and mechanical appliances	223	6%
Articles of apparel (knitted)	145	4%
Edible fruit and nuts	90	2%
Fish and crustaceans	88	2%
Plastics and plastic products	79	2%
Coffee, tea, mate and spices	73	2%

Source : https ://www.uktradeinfo.com/Statistics/BuildYourOwnTables/Pages/Table.aspx

Notes: Data presented is based on 2-digit HS codes.

1.27 Table 2 highlights both the UK's and Vietnam's revealed comparative advantages (RCA)[15]. The RCA estimates have been normalised to range between +1 and -1, where a positive RCA reflects a good which the UK exports relatively more compared to other countries, and a negative RCA identifies a good in which the UK exports relatively less than other countries.

1.28 The analysis shows that Vietnam tends to better at exporting products which the UK is not. The UK has a considerable advantage in the export of 'works of art and antiques', and in 'pearls, precious stones, and metals', whereas Vietnam's comparative advantages are focused on 'footwear', 'apparel', and 'vegetable products'.

Table 2: Revealed comparative advantage of UK and Vietnam goods exports

Product Category	UK RCA Normalised	Vietnam RCA Normalised
Works of art and antiques	0.82	-0.99
Pearls, precious stones and metals; coin	0.47	-0.79
Arms and ammunition	0.32	-1.00
Products of the chemical and allied industries	0.23	-0.68
Vehicles, aircraft and vessels	0.15	-0.69
Prepared foodstuff; beverages, spirits, tobacco	0.13	-0.04
Paper, paperboard and articles	0.07	-0.61
Instruments, clocks, recorders and reproducers	0.05	-0.24
Commodities not specified according to kind	-0.10	-1.00
Machinery and electrical equipment	-0.11	0.13
Base metals and articles	-0.13	-0.30
Live animals and products	-0.16	0.31
Mineral products	-0.16	-0.40
Resins, plastics and articles; rubber and articles	-0.17	-0.08
Articles of stone, plaster; ceramic prod.; glass	-0.24	0.00
Textiles and articles of apparel	-0.26	0.58
Miscellaneous manufactured articles	-0.26	0.30
Footwear, headgear; feathers, flowers, fans	-0.30	0.79
Hides, skins and articles; saddlery and travel goods	-0.32	0.46
Animal and vegetable fats, oils and waxes	-0.53	-0.48
Vegetable products	-0.59	0.51
Wood, cork and articles; basket ware	-0.73	0.36

Source: https://comtrade.un.org/data
Notes: The calculations are based on a 5-year average of 2012, 2013, 2014, 2015 and 2016 data, with the trade flow data extracted from Comtrade for goods categories.

[15] This is based on the Balassa Index (1965). It calculates the percentage of exports of a given sector in a given country and compares it to the equivalent measure of world trade. If a country has a greater share of its total trade in a given sector than the share of world exports in that sector, then it has a revealed comparative advantage in that sector.

1.29 Similarly, Table 3 shows the RCA's for UK and Vietnam service exports. The UK has a strong advantage in service areas which require high skilled workers - notably in the insurance and finance sectors. Vietnam's main advantage lies in travel reflective of its large tourism industry, whilst it also holds a small advantage in transport services.

Table 3: Revealed comparative advantage of UK and Vietnam service exports

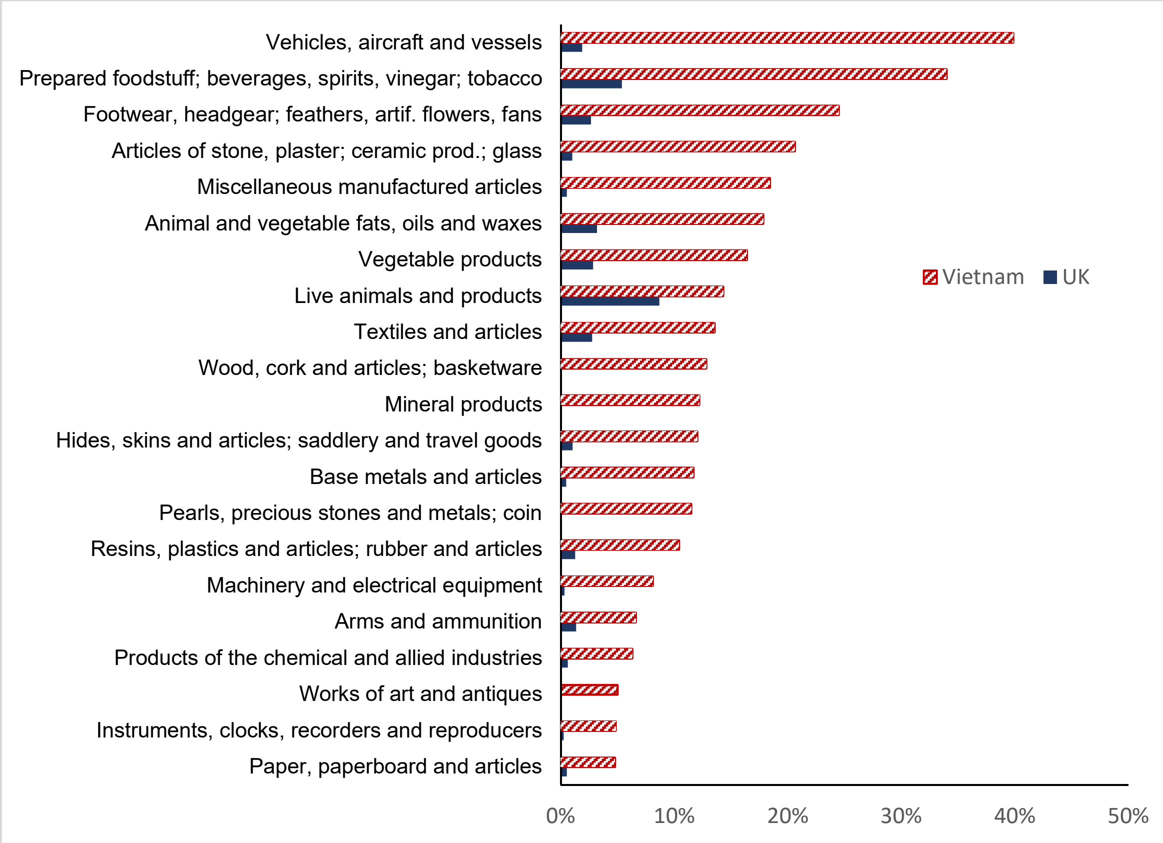
Service Category	UK RCA Normalised	Vietnam RCA Normalised
Insurance and pension services	0.52	-0.66
Financial services	0.46	-0.69
Personal, cultural, and recreational services	0.18	-
Other business services	0.12	-
Telecommunications, computer, and information services	-0.10	-0.75
Charges for the use of intellectual property	-0.10	-
Government goods and services	-0.13	-0.10
Transport	-0.25	0.07
Travel	-0.30	0.47
Maintenance and repair services	-0.34	-
Manufacturing services on physical inputs owned by others	-0.36	-
Construction	-0.37	-

Source: https://www.trademap.org
Notes: The calculations are based on a 5-year average of 2012, 2013, 2014, 2015 and 2016 data. '-' indicates that data is unavailable.

1.30 Tariffs or excise duties can be levied by a government to increase the cost of importing from abroad to protect domestic industries and/or raise revenue. The impact of a tariff depends on the behaviour and responsiveness of domestic consumers and businesses to a change in tariff. Graph 3, below, presents the trade weighted applied MFN tariffs imposed by Vietnam and the UK[16].

[16] Tariffs can be calculated as a simple average over a range of goods, which is the average tariff across several tariff lines. However, countries import different quantities of goods under different tariff lines which the simple average does not account for. A weighted tariff adjusts the average tariff for the volume of trade under each tariff line.

Graph 3: Trade weighted tariffs between the UK and Vietnam by sector



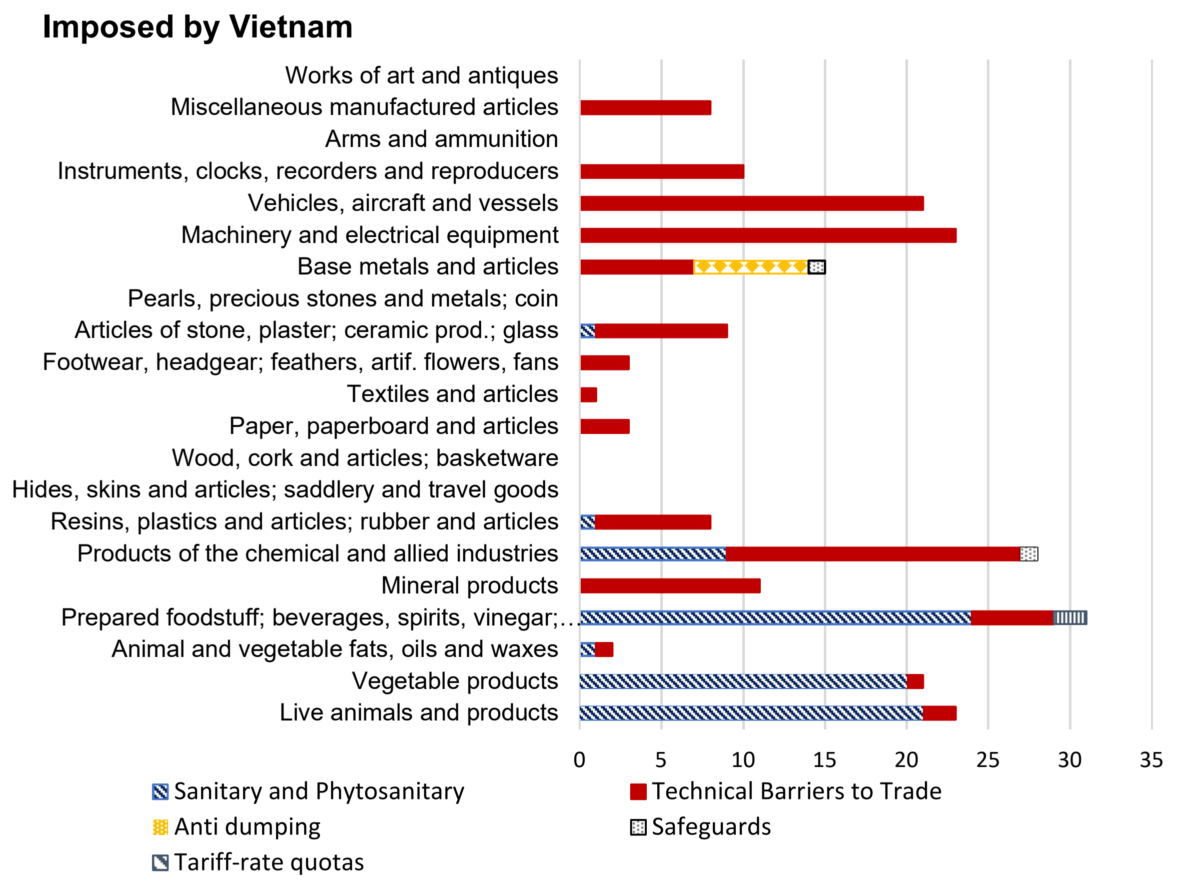
Source: International Trade Centre (ITC) market access maps. http://www.macmap.org/CountryAnalysis/.

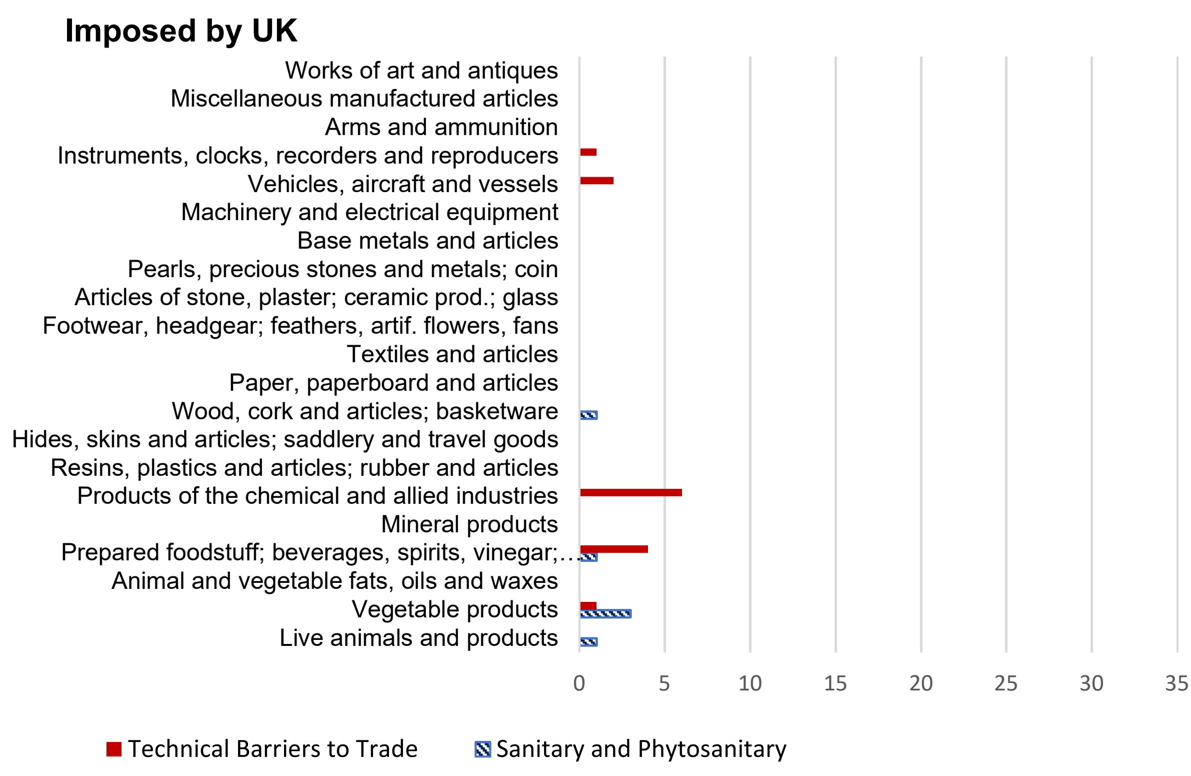
1.31 Graph 3 shows that there is a large disparity in the tariffs imposed by each country. On average, Vietnam imposes tariffs greater than 10% in 15 out of the 21 sectors listed. The UK does not exceed an average tariff of 10% in any sector. Vietnam's higher tariffs reflect its early stage of development, where protectionist policies may be in place to give industries space to develop. It is important to note that Vietnam can export to the EU under the Generalised Scheme of Preferences (GSP). This allows developing countries to pay lower or no duties on exports to the EU.[17]

1.32 Additionally, non-tariff measures such as regulatory and standards requirements can restrict the trade of goods and services. Graph 4, below, indicates that Vietnam imposes a larger amount and a greater variety of measures than the UK. It should be noted that Graph 4 only shows the number of NTMs imposed and not the extent to which they restrict trade.

[17] http://ec.europa.eu/trade/policy/countries-and-regions/development/generalised-scheme-of-preferences/index_en.htm

Graph 4: Number of NTMs imposed by Vietnam and the UK as of 2018 (pre-EVFTA)

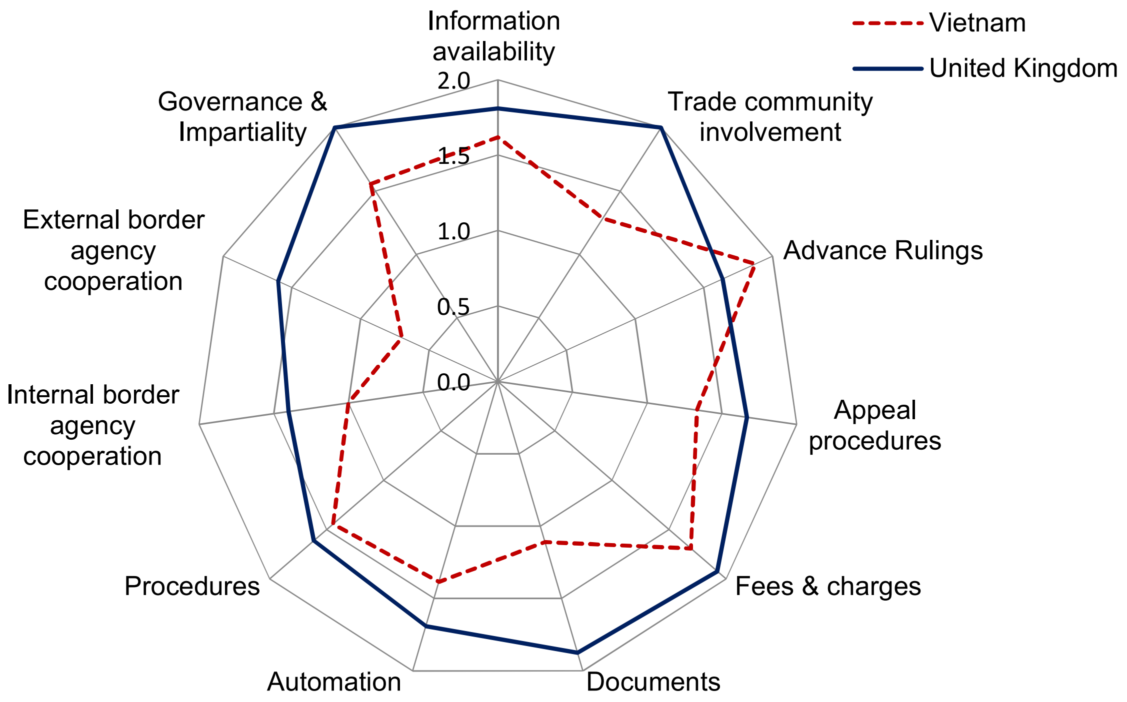




Source: WTO integrated analysis and retrieval of notified non-tariff measures

1.33 As well as tariffs and non-tariff measures, the complexity and cost of the trade transaction process can have an impact on overall trade flows. Graph 5, below, shows the Trade Facilitation Index (TFI) estimated by the OECD for the UK and Vietnam, which covers 11 indicators. Each indicator, such as automation of processes, is scored from 0 to 2, where 2 represents the best performance that can be achieved. With the exception of advance rulings, the data shows that the UK is much easier to trade with than Vietnam.

Graph 5: OECD trade facilitation index



Source: OECD (http://www.oecd.org/trade/facilitation/indicators.html)

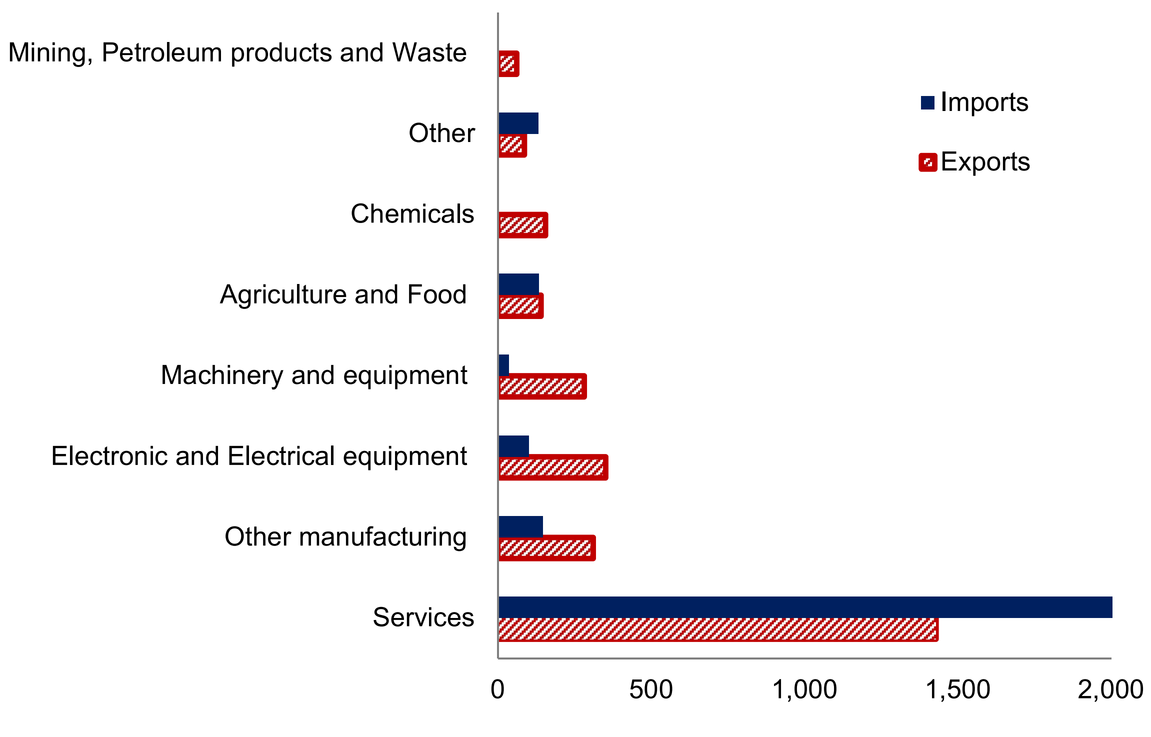
Notes:

A-Information Availability	Publication of trade information, including on internet and enquiry points.
B – Involvement of the Trade Community	The degree to which consultations are carried out with traders.
C –Advance Rulings	Prior statements by the government to requesting traders concerning the classification, origin, valuation method, etc., applied to specific goods at the time of importation; the rules and process applied to such statements.
D- Appeal Procedures	The ability to appeal administrative decisions by border agencies.
E – Fees and Charges	Disciplines on the fees and charges imposed on imports and exports.
F – Documents	Simplification of trade documents; harmonisation in accordance with international standards; acceptance of copies.
G – Automation	Electronic exchange of data; automated border procedures; use of risk management.
H – Procedures	Streamlining of border controls; single submission points for all required documentation (single windows); post-clearance audits; authorised economic operators.
I – internal cooperation	Co-operation between various border agencies of the country; control delegation to customs authorities.
J – External cooperation	Co-operation with neighbouring and third countries.
K – Governance and Impartiality	Customs structures and functions; accountability; ethics policy

1.34 In 2016, HM Revenue and Customs estimated there were 2,874 UK firms exporting goods to Vietnam and 2,611 UK firms importing goods from Vietnam. Graph 6, below, highlights the breakdown of businesses trading with Vietnam by sector. It should be noted that the values for 'motor vehicles,' 'aerospace,' and 'pharmaceuticals' have been supressed due to disclosure control procedure. In terms of goods trade, 'other manufacturing' has the highest number of firms importing from Vietnam (147), whilst 'electronic and electrical equipment' has the highest number of firms exporting to Vietnam (351).

1.35 Data is not available on the number of business that trade in services. The data presented as 'services' refers to trade in goods carried out by businesses classified as 'services'. When looking at the breakdown of UK businesses by industry, the service sector as a whole has the highest number of firms trading goods with Vietnam. In 2016, 1,429 UK service industry firms exported goods to Vietnam and 2,003 UK service industry firms imported goods from Vietnam.

Graph 6: UK businesses exporting to and importing from Vietnam in 2016



Source: IDBR overseas trade statistics country data tables 2016. https://www.gov.uk/government/statistics/uk-trade-in-goods-by-business-characteristics-2016.
Notes: The methodology used to compute these statistics is still under development by HMRC. All data should be considered experimental official statistics.

2 Strategic overview of the EVFTA

2.1 Vietnam is one of the fastest growing countries in ASEAN. Growth in Vietnam's economy is expected to continue and is expected to be around 5% in 2030. Vietnam has an increasingly open and trade-driven economy, and acts as a burgeoning advocate of free trade in the Asia-Pacific region. This is an encouraging trend, particularly given Vietnam's status as a developing country. Vietnam is indeed the only lower income country to be a member of the Comprehensive & Progressive Trans-Pacific Partnership (CPTPP), and the EVFTA itself is testament to Vietnam's commitment to negotiating ambitious and comprehensive liberalisation on a more equal footing with their trade partners, consciously moving away from reliance on unilateral preferences.

2.2 More broadly, Vietnam's centrality to trade and development relations in the region is both a cause and symptom of Vietnam's growing leadership within ASEAN. Vietnam has emphasised ASEAN's central role in facilitating regional dispute management and has been at the core of regional unity and stability. According to a recent Brookings Institute paper, "Vietnam has not only socialized quickly into the Southeast Asian community, but it has also proven capable of taking a more central role. Twenty years after joining ASEAN, Vietnam is arguably the most active player in the region in terms of foreign policy."[18]

2.3 The EU guide to EU-Vietnam Free Trade Agreement explains that bilateral trade and investment links between the EU and Vietnam have steadily strengthened since the two sides established formal diplomatic relations in 1996.[19] It goes on to explain how, for many years, the EU has been Vietnam's second most important two-way trading partner after China. The EVFTA provides business opportunity for engagement with Vietnam with its vibrant economy of more than 95 million consumers, a growing middle class and a young, dynamic workforce. The European Commission launched the negotiations for an ambitious and comprehensive free trade agreement with Vietnam in June 2012. Negotiations concluded in December 2015 and a text for the Agreement was published on 1 February 2016.

2.4 The primary aim of the EVFTA is to reduce barriers to trade and consolidate preferential trade access over the long-term, providing certainty to businesses and promoting economic growth, job creation and greater choice for consumers. The EVFTA aims to address specific concerns across a range of areas, including tariffs on goods, services market access, government procurement, intellectual property rights protection. Vietnam's developing country status has seen the EU accept a degree of asymmetry in negotiations. However, this has not reduced ambition from Vietnam on trade liberalisation under the FTA. Asymmetry concessions have primarily been made in the form of staging periods to allow certain provisions within the EVFTA to be gradually introduced over a number of years.

2.5 Along with these priorities, the EVFTA also includes a comprehensive chapter on trade and sustainable development (TSD), reaffirming obligations to respect universal human rights principles. It also contains a legally binding link to the EU-Vietnam Partnership and Cooperation Agreement (EVPCA), which includes a human rights clause and a provision for the right to take appropriate measures (including the suspension of agreements) in case of major violations.

2.6 Under the TSD chapter, Vietnam also committed to implement and ratify the three remaining core International Labour Organisation (ILO) conventions.[20] The Vietnamese are working with the ILO, and a draft decree is planned for 2019, with the conventions to being applied after the FTA enters into force (between 2019 and 2023). As part of their CPTPP commitments, Vietnam has a period of five years after the ratification of the agreement, during which it must implement conventions 87 and 98. As Vietnam intends to ratify the CPTPP agreement in autumn 2018, Vietnam will have until the end of 2023 to ratify all missing ILO conventions.

2.7 The Agreement will eliminate nearly all tariffs (over 99%), except for a small number of tariff lines for which the EU and Vietnam agreed on partial liberalisation through zero-duty Tariff Rate Quotas (TRQs). This is a far-reaching tariff elimination never before achieved with a developing country, but with adequate transition periods to allow Vietnam to adapt. Vietnam will liberalise 65% of duties on EU exports at entry into force, with the remainder of duties being gradually eliminated over a 10-year period. EU duties will be eliminated over a 7-year period.

2.8 The agreement also covers non-tariff barriers to trade and other trade related aspects including:

- Trade in Goods, including cars and pharmaceutical products
- Customs and Trade Facilitation
- Rules of Origin
- Technical Barriers to Trade
- Sanitary and Phytosanitary Measures
- Intellectual Property Rights
- Geographical Indications
- Services and E-commerce
- Investment
- Government Procurement
- Sustainable Development
- Renewable Energies
- Antitrust, Mergers, State-Owned Enterprises, Subsidies

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[18]Please see this link https://www.brookings.edu/opinions/vietnams-evolving-role-in-asean-from-adjusting-to-advocating/

[19] Please see this link http://trade.ec.europa.eu/doclib/docs/2016/june/tradoc_154622.pdf

[20] Conventions 87, 98 and 105 related to freedom of association, right to collective bargaining and elimination of forced labour.

- Trade Remedies and Dispute Settlements

2.9 EVFTA will enable UK firms to export and import at a lower cost and give more opportunity for UK businesses to bid for public procurement contracts in Vietnam. It will increase the welfare of UK households by lowering the price of goods and services and increasing consumer choice due to greater competition.

2.10 EVFTA also provides the basis for mutual recognition of conformity assessment bodies and acceptance of their test assessments to reduce the costs of such compliance for many sectors. However, EVFTA will not change EU standards and regulations such as those related to food safety, product safety, consumer protection, health, environment, social or labour standards. Without exception, all imports from Vietnam will have to continue to comply with EU product rules and regulations. Significantly in EVFTA, the EU and Vietnam resolved to preserve their ability to achieve legitimate policy objectives, such as public health, safety, environment, public morals and the promotion and protection of cultural diversity including the ability of governments to subsidise cultural activities.

2.11 After the Court of Justice of the European Union Opinion (CJEU) regarding the Singapore FTA and the division of competences between the EU and Member States, the EVFTA was revised to be an EU exclusive competence only agreement. This revised and final text was published in August 2018. The May 2017 CJEU Opinion on the EU-Singapore FTA (as drafted at that time) was that certain provisions within the draft investment chapter including mechanisms to resolve investor-state disputes were of shared competence between the EU and its Member States. The Commission and Vietnam subsequently removed the shared competence elements to enable EVFTA to be presented as an EU-only competence agreement. The investment protection element is presented as a distinct mixed Investment Protection Agreement (EVIPA). EVIPA has not been included in the scope of this impact assessment.

2.12 Separating the investment chapter from the rest of the agreement enables EVFTA as an EU-only competence agreement to enter into force in a more streamlined manner than a shared competence agreement. The EVIPA will need ratification by all EU Member States (which took close to five years with the EU-Korea FTA). As such we do not presently expect, both before the UK leaves the EU and during the proposed Implementation Period, there to be any impact on investors or the UK and Vietnam as a result of the EVIPA. The UK-Vietnam Bilateral Investment Treaty (BIT) remains fully in force.

2.13 The EVFTA also supports a long-term secondary objective of a regional FTA between the EU and ASEAN. The EVFTA, EVIPA, the EU-Singapore FTA and IPA act as benchmarks for further ASEAN agreements, setting the scope and ambition for further bilateral EU FTAs with countries across the region and an overarching EU-ASEAN FTA in the long-run. [21]

3 Problem under consideration

3.1 The European Commission has presented a proposal on signature and conclusion of this Agreement to the Council of the European Union.

3.2 The Council will now decide whether to formally adopt the necessary Council Decision authorising signature and conclusion of the Agreement. In the past, Council Decisions on signature of EU trade agreements have typically been agreed through Common Accord, requiring the agreement of all Member States. We expect this to be the approach followed for the EU-Vietnam FTA.

3.3 The UK Government has to establish its position on this (which will be subject to UK Parliamentary scrutiny).

[21] Within the ASEAN region, the EU is currently negotiating a bilateral FTA with Indonesia. Negotiations with Malaysia, Thailand, the Philippines and Burma are on hold.

4 Rationale for intervention

4.1 As a global champion of free trade, the UK government has long supported initiatives liberalising the trading landscape. On this basis the UK welcomes the EU's ambitious and extensive FTA agenda and continues to support the full range of EU FTAs as a means of driving economic growth, creating jobs and promoting consumer choice. The EVFTA can contribute positively to this overarching objective.

4.2 UK Government support for the signature of EVFTA would be a demonstration of this commitment, and a positive move by the UK as an EU Member State in demonstrating support for Vietnam and for global trade.

4.3 The rationale for intervention is to provide UK support for the entry into force of the agreement, and to realise the benefits for the UK and Vietnam described in this impact assessment. The range of tariff and non-tariff barriers that the agreement seeks to address should help to improve bilateral trade flows, provide certainty for UK businesses and make it easier for our companies to operate in the Vietnamese market. Failure to do so could see the EU and Vietnam continue to trade on WTO MFN terms, which is not the Government's preferred option.

4.4 The Government seeks continuity in the UK's existing trade relations when it leaves the EU, including continuity of existing EU FTAs such as the EVFTA, to avoid disruption for businesses and consumers. UK support for the EVFTA at the Council will demonstrate the UK's commitment to this agreement and provide clear endorsement for continuing the provisions once the UK leaves the EU.

4.5 Abstention in any vote in Council on signature and conclusion of the agreement, could prevent common accord. Such action might be seen as a failure by the UK to demonstrate a duty of sincere cooperation as an EU Member State. It would also send a negative signal to the global trading community about UK support for rules-based international free trade and, specifically, to Vietnam.

5 UK policy objectives

5.1 The UK has always been deeply committed to free and open international trade and investment as drivers of growth, prosperity, jobs, and consumer choice. Trade has lifted millions out of poverty, and supports peace and promotes security. It is well established that trade is beneficial to both partners to a trade agreement, through:

- more consumer choice in the variety and quality of goods and services,
- lower prices through increased competition and efficiency
- higher productivity and,
- higher real wages and living standards for the countries engaged.

5.2 Free trade agreements, such as the EU-Vietnam FTA aim to increase trade and reduce trade barriers.

5.3 The UK's policy objectives are to support the EU's ambitious trade agenda and as part of this support the signature and implementation of EVFTA to promote bilateral trade and increase economic growth. This will be achieved by a) eliminating most tariffs and b) reducing non-tariff measures that businesses face when trading goods and services and when investing abroad. The EVFTA will enable UK firms to export and import at a lower cost and give more opportunity for UK businesses to bid for public procurement contracts in Vietnam. Furthermore, the EVFTA will increase the welfare of UK households by lowering the price of final goods and services and increase consumer choice due to greater competition.

5.4 As well as promoting bilateral trade and growth in Vietnam, the UK's ratification of EVFTA would:

- Provide a practical demonstration to the EU of the UK's commitment to support EU trade policy whilst still a Member State;
- Demonstrate our support to Vietnam;
- Demonstrate the Government's intention to work with Vietnam to ensure continuity in our trading relationship after UK EU exit.

5.5 The Government is committed to maintaining continuity of trade relations to deliver certainty and stability for businesses and consumers when we leave the EU. UK support for EVFTA at the Council will demonstrate the UK's commitment to this agreement and provide clear endorsement for continuing the provisions once the UK leaves the EU.

5.6 Overall, the Government supports the EVFTA and advocates swift implementation of the agreement.

6 Description of options considered

6.1 Two options have been considered, with evaluation against a baseline where EVFTA is not in force.

Option 1: UK supports signature and conclusion of the EVFTA

6.2 The Government's preferred option is for the UK to vote in favour of signature and conclusion of the EVFTA so that it can be implemented (pursuant to approval from the European Parliament and ratification by Vietnam).

Option 2: UK does not support signature and conclusion of EVFTA

6.3 The other option is for the UK to not support signature and conclusion of the agreement. In this case, the means by which Council vote could have a bearing on the outcome.

6.4 Should Council approval be sought via Common Accord, failure by one or more Member States to vote in favour would prohibit the agreement from being signed and concluded. Whilst in practice there could be scope to engage in dialogue to try to unblock signature, the practical impact of the EVFTA not being signed and concluded would be the EU and Vietnam continuing to trade on WTO, Most Favour Nation (MFN) terms and, for Vietnam, under the Generalised Scheme of Preferences. Under this option the UK does not accrue any additional costs and benefits. This is the baseline of this IA.

6.5 Should Council Approval be sought alternatively via Qualified Majority Vote, failure by the UK to support signature would not itself stop the Council reaching agreement on EVFTA being signed if a sufficient number of other Member States vote in favour. The impact then would be a delay to the accrual of benefits, which we cannot quantify, and presentational issues.

7 Monetised and non-monetised costs and benefits of each option

7.1 This section will look in depth at the costs and benefits of each policy option under consideration, focussing on the impacts to UK businesses, consumers, and the wider economy.

7.2 Most of the results reported in this section are derived from Computable General Equilibrium (CGE) modelling. This type of modelling is appropriate when there is a significant change in trade policy and an assessment of the impacts on the whole economy is needed. The model considers linkages between domestic markets within each economy and provides impacts at a sectoral and aggregate level. It also considers the knock-on consequences to trade flows of third parties, reflecting trade creation and trade diversion effects, as well as the allocation of resources within an economy.

7.3 **CGE analysis can provide a useful indication of the potential magnitude of economic impacts resulting from policy changes. CGE results should not, however, be treated as a forecast or prediction of the future.** Annex A lays out further details on CGE modelling.

Economic appraisal the EU-Vietnam Free Trade Agreement on the UK

7.4 We draw on external evidence from "The impact of the EU-Vietnam FTA on the UK" (2019), a study commissioned by DIT and conducted by Paul Baker and David Vanzetti.[22] The estimates in this external study are based on the authors' interpretation of the EVFTA text and their judgement on the additional market access offered under the agreement. The assumptions used in their study are therefore subject to a degree of uncertainty. The economic analysis presented in the external study cannot fully capture the comprehensiveness and complexity of the EVFTA. Nonetheless, this is the best available source to examine the impacts of EVFTA for the reasons set out below:

i. This study specifically looks at the impact of the FTA on the UK. This reduces the need to make assumptions around the proportion of the EU benefits attributable to the UK.

ii. The study applies a CGE model which shows the impacts of a trade agreement across the whole economy rather than in one specific sector.

iii. This study applies a dynamic model, meaning we are able to understand how benefits accrue over time.

iv. This study assumes different levels of service liberalisation across different sectors based on the content of the final EVFTA text.

[22] Source: Baker and Vanzetti (2019). *'Impacts on the United Kingdom of the EU-Vietnam FTA'.*

7.5 As mentioned above, there are limitations of the external study. As well as being based on the authors' interpretation of the EVFTA text and their judgement on the additional market access offered under the agreement, the study does not explore the microeconomic (firm level), environmental and social impacts of the EU-Vietnam FTA. In addition, the analysis is based on the structure of the Vietnamese and UK economies in 2014.

7.6 We set out the impacts of the EVFTA on UK GDP, bilateral exports, bilateral imports, total exports and total imports as well as sectoral effects. We also use this study to assess the impacts on consumer prices and domestic output. The estimated impacts can vary depending upon the assumptions built into CGE modelling.

Key assumptions

- The baseline is one where the EVFTA is not in force across the EU28 and Vietnam. Under the baseline scenario the EU28 trades with Vietnam under the Most Favoured Nation commitments agreed at the WTO and not under the preferences contained in the EVFTA. The modelling assumes Vietnam trades with the EU28 under the GSP and therefore at a lower tariff rate than the MFN rate.

- For modelling purposes, the EU and UK continue to trade on current terms and the UK and Vietnam trade on equivalent preferential terms as those set out in the EVFTA for the duration of the assessment period after the UK has exited the EU. It is the Government's intended policy to ensure continued access to the preferences set out in the EVFTA after the UK leaves the EU.

- The impact of the trade agreement is modelled over a 10 year period up to 2030. Tariff eliminations negotiated in the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), Comprehensive Economic and Trade Agreement (CETA) between the EU and Canada and the EU-Singapore FTA are factored into the baseline. However, the reduction in regulatory barriers to trade negotiated in these agreements are not included in the baseline. See Annex B for information on how the Comprehensive and Progressive Trans Pacific Partnership (CPTPP) could affect this baseline.

- The baseline data underpinning the CGE analysis captures the pattern of world trade up to 2014. Since then, the EU has concluded several trade agreements including the Comprehensive Economic and Trade Agreement (CETA) between the EU and Canada and the EU-Singapore FTA. Equally Vietnam is a member of the Comprehensive and Progressive Trans Pacific Partnership (CPTPP) and is currently in the process of ratifying the trade agreement. These agreements could result in trade diversion between the UK and Vietnam. Baker and Vanzetti (2019) account for tariff eliminations set out in these FTAs to provide a better assessment of the EUVFTA on the UK economy.[23]

- Agreements not yet in force (EU-Singapore) have been included in the baseline to ensure that the modelling can provide a more accurate assessment of the impact of the EVFTA between now and 2030.

- The baseline cost to trade in services is based on the study produced by the World Bank published in 2014.[24]

- The degree to which the EVFTA reduced service regulatory barriers to trade is based on the Baker and Vanzetti's assessment of the agreement text.

- Baker and Vanzetti (2019) use the United Nations Conference on Trade and Development (UNCTAD) NTM dataset to estimate the baseline degree of regulatory alignment between the UK and Vietnam on goods trade. The authors estimate the scope for further regulatory convergence, as a result of the EVFTA, using econometric regression analysis.

[23] See Annex B for information on how the Comprehensive and Progressive Trans Pacific Partnership (CPTPP) could affect this baseline.

[24] http://documents.worldbank.org/curated/en/137321468331910699/Estimates-of-ad-valorem-equivalents-of-barriers-against-foreign-suppliers-of-services-in-eleven-services-sectors-and-103-countries

Assessment of option 1: UK supports signature and conclusion of the agreement and it is implemented

Overall benefits to the UK Economy

7.7 Compared to a baseline in which the EVFTA is not in force, **the beneficial impact of the EVFTA on UK GDP is estimated to be around £390 million (0.01%) in the long run.** UK exports to, and imports from, Vietnam are estimated to increase by £490 million (60%) and £1.7 billion (33%) respectively per annum in the long run. As set out in section 2, the UK had a trade deficit with Vietnam in 2016. The implementation of the EVFTA is expected to increase the UK's trade deficit with the Vietnam. It is important to note that gains in UK imports from Vietnam will result in lower UK input production cost for UK businesses and lower prices for UK consumers. See Annex C for further details on the factors affecting GDP. As mentioned above, the estimates in the external study are based on the authors interpretation of the EVFTA text and their judgement on the additional market access offered under the agreement and is therefore subject to a degree of uncertainty.

7.8 The sectors in the UK that are expected to experience the greatest increase in exports to Vietnam are financial and insurance services (£110 million, 48% increase), business services (£80 million, 50% increase) and air transport (£80 million, 118% increase). UK business are also expected to gain from cheaper imports from Vietnam. UK imports from Vietnam are expected to increase by the greatest amount in wearing apparel (£530 million, 78% increase), leather (£460 million, 94% increase) and motor vehicles and transport equipment (£400 million, 17% increase). UK total exports to, and total imports from, the world are estimated to increase by £350 million (0.09%) and £120 million (0.01%) per annum respectively in the long run. Consumer welfare is expected to increase £290 million per annum. The net impact of EVFTA on UK GDP is accounted for in the total Net Present Value (NPV) of the agreement presented in Section 9.

7.9 The benefits identified under this policy option are expected to outweigh the costs relating to one-off familiarisation costs, ongoing compliance costs, foregone benefits to government revenue, and the additional administration needed to trade under EVFTA preferences. **The government's preferred option is to see the EVFTA enter into force in order for the UK to gain these benefits.**

7.10 The section below assesses the direct and indirect impacts of EVFTA on UK businesses, UK consumers, the UK Exchequer and wider impacts. We define direct impacts as those that automatically affect businesses, customer and the UK Exchequer and does not assume any behavioural change. For example, the removal of Vietnamese regulations allows UK business to export to Vietnam automatically at a lower cost. In comparison, indirect impacts are those that require a behavioural response from businesses. For example, UK firms may increase domestic production to increase their exports to Vietnam.

The net impacts of EVFTA to UK businesses

a) Direct benefits to UK businesses from a reduction in tariffs and regulatory barriers to trade

(i) Monetised impacts

7.11 UK businesses will benefit from reduced tariffs and non-tariff barriers on both exports to and imports from Vietnam. As a result, UK goods and services will be more price competitive in Vietnam. UK producers will be able to import a greater choice of intermediate goods and services at a lower cost. The following section outlines the additional market access that firms will receive upon the EVFTA's entry into force.

Tariff and non-tariff barrier reductions in the trade of goods

7.12 EVFTA dismantles nearly all tariffs except for a few lines that are subject to duty-free tariff rate quotas. At entry into force, 65% of EU exports to Vietnam will be duty free. The remaining trade, with the exception of a few products, will be liberalised after 10 years. The elimination of tariffs is treated as a transfer as the reduction of cost to UK businesses is a revenue that otherwise would have been gained by the UK Exchequer. The agreement will eliminate 99% of all tariffs currently impose by Vietnam and the EU in the long run.

7.13 The table below sets out how the tariffs imposed by the EU and Vietnam change after the implementation of the EVFTA. In general, Vietnam's average tariffs on goods are higher than those imposed by the EU. The most significant tariff cuts to Vietnam's schedule are seen for rice (10.8 percentage point tariff reduction) and wearing apparel (9.3 percentage point tariff reduction). Sectors which will still be relatively protected in Vietnam are pork and poultry where the tariff will be at 12.1%. The largest tariff reductions by the EU and therefore the UK can be seen in beverages and tobacco (27.8 percentage point reduction), wearing apparel, sugar and textiles (full tariff elimination for all).

Table 4: Changes in tariff schedules						
	Vietnam's tariffs on UK/EU goods			UK/EU tariffs on Vietnam's goods		
	Baseline* (%)	**Tariffs in 2030 post EVFTA (%)**	**Percentage point change**	**Baseline* (%)**	**Tariffs in 2030 post EVFTA (%)**	**Percentage point change**
Rice	23.4	12.7	-10.8	-	-	-
Wearing apparel	9.3	0.0	-9.3	17.4	0.0	-17.4
Leather	6.9	0.0	-6.9	9.5	2.2	-7.3
Food products	6.3	0.0	-6.3	7.5	1.5	-6.0
Textiles	4.5	0.0	-4.5	10.5	0.0	-10.5
Pork and poultry	16.0	12.1	-3.9	6.6	1.5	-5.1
Beverages & tobacco	4.7	1.5	-3.2	44.0	16.2	-27.8
Motor vehicle & trans equip	2.7	0.0	-2.7	26.6	11.7	-14.9
Fishing	2.7	0.0	-2.7	8.7	0.0	-8.7
Sugar	2.6	0.0	-2.6	12.6	0.0	-12.6
Chemical, rubber & plastics	1.8	0.4	-1.4	2.8	0.0	-2.8
Mineral products	0.9	0.2	-0.7	7.8	0.0	-7.8
Manufactures	0.1	0.0	-0.1	5.3	0.0	-5.3
Vegetables, fruit, nuts	0.1	0.0	-0.1	5.6	0.0	-5.6
Other crops	0.03	0.02	0.0	4.5	2.7	-1.8
Petroleum, coal products	-	-	-	7.8	0.1	-7.7
Paper products, publishing	-	-	-	6.8	0.0	-6.8
Beef and veal	-	-	-	6.2	0.0	-6.2
Dairy products	-	-	-	11.6	7.6	-4.1
Electronics	-	-	-	2.5	1.0	-1.5
Forestry	-	-	-	0.5	0.0	-0.5
Machinery and equipment	-	-	-	3.5	0.0	-3.5
Minerals	0.01	0.01	N/A	2.6	0.0	-2.6
Wood products	0.1	0.1	N/A	1.3	0.0	-1.3
Ferrous metals	0.03	0.03	N/A	0.9	0.5	-0.4
Resources	-	-	-	-	-	-

Source: Baker and Vanzetti (2019)
Notes: Vietnam’s baseline tariffs on EU imports reflect MFN tariffs whereas the EU’s baseline tariffs on imports from Vietnam reflect GSP tariffs.

7.14 **Machinery and mechanical appliance** products are the largest UK goods export to Vietnam. UK exports were £107 million on average between 2015 to 2017 and accounted for 22% of all UK exports to Vietnam. Under the EVFTA, the 3.5% tariff imposed on UK exports in machinery and mechanical appliance will be eliminated.

7.15 **Pharmaceutical** products are the second largest UK goods exports to Vietnam and accounted for 12% of total UK exports to Vietnam on average between 2015 to 2017. UK exports to Vietnam in pharmaceutical products over this period were on average £56 million per annum. Under the EVFTA, Vietnam's WTO tariffs on pharmaceutical products (up to 8%) will be fully eliminated.[25]

7.16 **Automobiles –** EVFTA provisions improve market access for European cars entering Vietnam. Investment and manufacturing of motor vehicles and transport equipment will remain restricted, but tariffs on EU cars (up to 78%) will be reduced to zero after 10 years and on car parts to zero after 7 years.[26] The EVFTA contains an annex devoted to Non-Tariff Measures (NTMs) in the automobile sector which comes into effect three years after entry into force. The agreement builds on the 1958 United Nations Economic Commission for Europe (UNECE) agreement which sets out a common set of technical prescriptions and protocols for type approval of vehicles and components. As a result, Vietnam will accept on its market EU parts and equipment complying with UNECE regulations. Furthermore, Vietnam will discontinue its requirements for conformity of production reports.

7.17 **Alcoholic beverages –** Vietnam imposes relatively high tariffs on alcoholic beverages (50% on wine and 48% on spirits).[27] Both wine and spirits can be traded duty free after 7 years from entry into force and tariffs on beer exports will be eliminated after 10 years. The UK exported £9 million in alcoholic beverages to Vietnam on average between 2015 to 2017. These products can be traded at a lower cost under the EVFTA.

7.18 **Clothes (wearing apparel) and textiles –** the EVFTA fully eliminates tariffs faced by UK exporters of clothes (17.4 percentage point reduction) and textile products (10.5 percentage point reduction). On average between 2015 to 2017, the UK exported around £7.5 million in clothing to Vietnam.

7.19 The UK imported just under £500 million in clothes and material (wearing apparel) on average between 2015 and 2017 and accounted for 13% of all UK imports from Vietnam. Under the EVFTA, the EU's average MFN tariffs on these products (9.3%) are fully eliminated. UK businesses are therefore expected to benefit from a reduction in input costs. These gains may be transferred to UK consumers in the form of lower prices.

[25] Main Benefits report http://trade.ec.europa.eu/doclib/press/index.cfm?id=1919.

7.20 **Leather products** – The EU's MFN tariffs on leather products (6.9%) will be fully eliminated under the EVFTA. The UK's second largest imports from Vietnam was footwear (£454 million imports on average from 2015 to 2017) and accounted for 12% of all UK imports from Vietnam. UK businesses are expected to benefit from a reduction in cost associated with footwear and other leather products. These gains may be transferred to UK consumers in the form of lower prices.

Non-tariff barrier reductions in the trade of services

7.21 The EVFTA aims to better align the regulations imposed on service trade between the EU and Vietnam. The FTA is expected to significantly open up access to Vietnam's services sector. EU barriers to trade in services are generally quite low. The EVFTA does however provide Vietnam more access to the EU market for business and transport services.

7.22 **Financial services -** Vietnam commits to cross-border services for financial data processing, advisory and intermediation and other auxiliary financial services. At present EU businesses can own a maximum of 30% of all shares in Vietnamese banks. Under the EVFTA EU businesses will be able to increase this share to 49%.

7.23 **Business services -** The agreement provides better access in a number of business sub-sectors. In sectors such as building cleaning, nursing and physiotherapy services, Vietnam has offered new market access opportunities to EU firms. Vietnam also abolished limitations in a number of business services (e.g. architectural, urban planning and urban landscape architectural services).

7.24 **Distribution services -** Five years after the entry into force of the agreement, Vietnam will stop requiring retailers to carry out an economic needs test (ENT) when opening outlets. Until then, retailers will only need an ENT for their first outlets (stores < $500m^2$). In addition, Vietnam commits to ensure that the existing licensing of spirits will not become more restrictive.

(ii) Non-monetised impacts

7.25 **Pharmaceuticals** - Vietnam will allow foreign pharmaceutical companies to establish enterprises in order to import pharmaceuticals that have been authorised to be sold on the Vietnamese market. Such foreign-invested enterprises will be allowed to:

- Sell pharmaceuticals imported by them to distributors or wholesalers in Vietnam
- Build their own warehouses

[26] Main Benefits report ht/trade.ec.europa.eu/doclib/press/index.cfm?id=1919.

[27] Main Benefits and Agriculture report http://trade.ec.europa.eu/doclib/press/index.cfm?id=1919.

- Provide information about their product to health care practitioners and do clinical study and testing.

7.26 **Government procurement** - After a transitional period of two years from entry into force, EU suppliers will be allowed to bid for government contracts. From that point the share reserved for domestic suppliers/producers will diminish over 15 years to a final share of 50%. The remainder will be open to all suppliers with market access rights. Further to this, provisions on international property rights will make Vietnam more attractive for producers of pharmaceutical products, such as:

- Vietnam will provide regulatory data protection to pharmaceutical (as well as to agri-chemical products) for five years.
- It will also provide an extension of patent protection, up to a limit of two years, to compensate for delays in the marketing approval of pharmaceutical products if the approval process takes more than 24 months.
- Vietnam will withdraw existing clinical trials requirements on ethnicity.

7.27 **Geographical indicators –** Under EVFTA various geographical indicators will be protected upon entry into force of the FTA including ‘Rioja’, ‘Ouzo’ and ‘Grappa’. Of particular interest to the UK is the protection afforded to ‘Scotch Whisky’, ‘Scottish Farmed Salmon’, ‘Irish Whiskey’ and ‘Irish Cream’.

7.28 **Technical barriers to trade (standards) –** EVFTA includes commitments for Vietnam to:

- Encourage standardising bodies to participate in the preparation of international standards by relevant international standardising bodies.
- Use relevant international standards as a basis for the development of domestic standards.
- Avoid duplication of, or overlap with, the work of international standardising bodies.
- Review national and regional standards not based on relevant international standards at regular intervals, with a view to increasing their convergence with relevant international standards.
- Notify technical regulations and conformity assessment procedures making voluntary standards mandatory.

7.29 **Technical barriers to trade (conformity assessment) –** EVFTA includes commitments for Vietnam to:

- Recognise EU certificates of conformity assessment on cars.
- Ensure that businesses have a choice amongst conformity assessment facilities and ensure that there is independence and no conflicts of interest between accreditation bodies and conformity assessment bodies.
- Consider joining or encourage its testing, inspection and certification bodies to join any functioning international agreements or arrangements for

harmonisation and/or facilitation of acceptance of conformity assessment results.

(b) Indirect benefits to UK businesses from a reduction in trade barriers

(i) Monetised impacts

7.30 Analysis produced by Baker and Vanzetti (2019) estimates **the EVFTA could increase UK exports to Vietnam by approximately £490 million per annum (60%) in the long run**. This represents a situation where the full effects of the agreement have been reflected in the economy (in 2030) compared against a baseline where EVFTA is not in force for EU28 or Vietnam.

7.31 The elimination of tariffs and reduction in service regulatory barriers improve market access opportunities for UK businesses to the Vietnamese market. Table 5 presents the top 10 UK sectors that gain the most in total exports from EVFTA. Most of the export gains are in services, accounting for £430 million of the £490 million increase in bilateral exports gains to Vietnam. We expect the gains in the service sectors to be the upper end scale of the impacts.

7.32 The top 10 sectors make up around 90% of the estimated increase in UK exports to Vietnam. Baker and Vanzetti (2019) find that exporters of financial & insurance (+£110m), business services (+£80m), air transport (+£80m) and communication (+£50m) will gain the most from an increase in exports to Vietnam. As Table 5 shows the monetised impacts of the EVFTA and the associated increases in UK total exports to the world are modest. However, the EVFTA is estimated to significantly increase UK exports to Vietnam in percentage terms across a number of sectors.

7.33 The modelling results provide a useful indication of the plausible magnitude of impacts, and sectors where the impacts might be greatest, but the specific figures should not be treated as a forecast or prediction of the future.

Table 5: Top 10 UK sectors export gains in goods and services in 2030 with EVFTA				
	Change in UK export to Vietnam per annum		Change in UK total world exports per annum	
Sector	**Monetised change**	**Percentage change**	**Monetised change**	**Percentage change**
Finance & insurance	£110 million	48%	£90 million	Marginal increase
Business services	£80 million	50%	£20 million	Marginal increase
Air transport	£80 million	118%	£70 million	Marginal increase
Communication	£50 million	145%	£50 million	Marginal increase
Retail & wholesale trade	£30 million	145%	£30 million	Marginal increase
Other transport	£20 million	134%	£20 million	Marginal increase
Other services	£20 million	61%	£20 million	Marginal increase
Recreation and other services	£20 million	49%	£20 million	Marginal increase
Chemical, rubber & plastics	£20 million	37%	£10 million	Marginal increase
Sea transport	£10 million	72%	£10 million	Marginal increase
Total top 10 bilateral exports	**£450 million**			
Total increase in exports	**£490 million**		**£390 million**	
Total increase in net exports	**£490 million**	**60%**	**£350 million**	**0.09%**

Source: Baker and Vanzetti (2019)
Notes: Figures are presented in 2017 prices and may not sum due to rounding.
Total increase in net exports captures sectors which experience an increase and decrease in exports.

7.34 The EVFTA is estimated to increase UK imports from Vietnam by £1.7 billion due to favourable preferential rates. Although the monetised impact is significantly larger for imports compared to exports, it is smaller in percentage terms. The increase reflects a 33% increase in UK imports from Vietnam. This could lead to lower UK business costs for intermediate products. The elimination of tariffs and the reduction in service regulatory barriers means UK businesses are expected to be able to purchase goods and services at a lower cost compared to the baseline, resulting in higher profits or lower consumer prices.

7.35 The table below shows the top 10 sectors in the UK that will import more goods and services from Vietnam as a result of EVFTA. The main sectors in which the UK will import more from Vietnam are wearing apparel (clothes and materials) (+£530m), leather products (+£460m) and motor vehicle and transport equipment (+£400m).

7.36 Whilst bilateral trade is estimated to increase significantly as a result of the FTA (60% for exports and 33% for imports), the impact is much smaller on national trade 0.9% for total UK exports and 0.1% for total UK imports. As the FTA offers preferential access bilaterally, UK trade is diverted away from other destinations to Vietnam.

Table 6: Top 10 UK sectors import gains in goods and services				
	Change in UK imports from Vietnam per annum		Change in UK total world imports per annum	
Sector	**Monetised change**	**Percentage change**	**Monetised change**	**Percentage change**
Wearing apparel	£530 million	78%	No change	
Leather	£460 million	94%	Marginal increase	
Motor vehicle & trans equip	£400 million	17%	No change	
Business services nec	£140 million	185%	Marginal increase	
Food products nec	£60 million	24%	Marginal increase	
Textiles	£40 million	55%	Marginal increase	
Air transport	£30 million	66%	Marginal decrease	
Finance & insurance	£20 million	45%	Marginal increase	
Chemical, rubber & plastics	£10 million	8%	Marginal increase	
Other transport	£10 million	98%	Marginal increase	
Total top 10 bilateral imports	**£1.70 billion**		**£6 million**	
Total increase in imports	**£1.78 billion**		**£150 million**	
Total increase in net imports	**£1.72 billion**	**33%**	**£120 million**	**0.01%**

Source: Baker and Vanzetti (2019)
Notes: Figures are presented in 2017 prices and may not sum due to rounding.
Total increase in net imports captures sectors which experience an increase and decrease in imports.

(ii) Non-monetised impacts

7.37 Trade liberalisation will increase UK business productivity by increasing competition. UK businesses can specialise in the production of goods and services that they are relatively better at producing, allowing them to expand production, benefit from economies of scale and produce goods at a lower average cost. In addition, UK businesses will have the incentive to reduce costs and increase efficiency in the face of greater international competition.

7.38 There are several channels through which competition raises productivity, but most importantly competition forces firms to innovate, coming up with new products and processes which can lead to step-changes in efficiency.

c) Direct costs to UK businesses

(i) Monetised impacts

7.39 Trading under EVFTA preferences is voluntary. UK business have the option to choose whether to trade with Vietnam under EVFTA preference (i.e. under lower tariffs) or the baseline MFN tariffs. Therefore, there is no net cost to businesses for those who do not wish to trade under EVFTA preferences.

7.40 We attempt to monetise the direct cost to businesses where possible for both one–off and ongoing costs. It is difficult to estimate business costs due to availability of data and there are considerable uncertainties around the cost estimates provided. For this reason, we provide ranges where possible and a description of the costs and activities involved to demonstrate the impact on businesses. Our best estimate of business impact costs has then been included in the Total NPV calculations. There are some limitations to the data used in this section, these include:

- Data on the preference utilisation of trade deals is not readily accessible. This means that existing evidence on preference utilisation is limited.
- HMRC empirical data on the administration costs incurred by businesses to trade are commercially sensitive and not available for this analysis.

7.41 There will be one-off costs to firms, enforcers, and customs and government officials from reading and understanding the text of this agreement. It is not possible to monetise the precise impact of this one-off cost, but we provide an illustration of the potential impacts on UK businesses that trade with Vietnam. In 2016, HMRC estimated that around 2,900 VAT registered businesses exported goods to Vietnam and around 2,600 VAT registered businesses imported goods from Vietnam. Based on this, the upper bound of businesses that could be trading with Vietnam in goods is 5,500 in 2016. This figure could be an overestimate as it double counts firms who both export to Vietnam as well as import from Vietnam. However, it does not consider the number of new businesses that may trade with Vietnam as a result of EVFTA which may lead to an underestimate. Secondly and importantly it does not capture the number of business that trade in services which will lead to an underestimation.

7.42 Based on this number of firms, the aggregate cost to businesses currently trading with Vietnam could range from £1.3 to £1.4 million. The method for this estimate is shown in Annex D. Our central estimate of business impact costs are included in the NPV calculations in section 9.

(ii) Non-monetised impacts

7.43 To trade under the EVFTA preferences, business are required to produce a certificate to confirm the origin of the export content meets the rules of origin requirements set out in the agreement. Businesses can submit rules of origin forms to HMRC to process free of charge however this could take several days to complete. Alternatively, businesses can choose to get an origins certificate from the British Chambers of Commerce which processes the certificate in a shorter period for a fee of £52.20.[28]

7.44 Recent academic studies (World Bank 2014, Ciuriak & Xiao 2014) estimate the tariff equivalent trade costs associated with rules of origin administration and compliance requirements ranges between 2% to 6%. These estimates vary considerably depending on the methodology, time period, and the countries under consideration. Further research (Keck and Lendle 2012) has shown that utilisation of agreements can be very high, even where there are very small preferential margins, which could not be the case in the presence of high administrative costs.

7.45 Firms could face other one-off costs such as IT set-up costs and custom declarations.

d) Indirect Costs to UK businesses

(i) Monetised impacts

7.46 There are no monetised indirect impacts to UK businesses

(ii) Non-monetised impacts

7.47 UK business will be exposed to greater international competition with greater trade liberalisation. This may cause a decline in production for domestic businesses that are less competitive. However, due to data limitations it is not possible to indicate which sectors may incur a decline in activity.

[28] https://www.londonchamber.co.uk/cofo/ January 2019 Price List.

Impact on Consumer welfare

a) Direct benefits to UK consumers

7.48 UK consumers will be able to imports products at a lower cost due to the tariff reduction on final goods. This can be viewed as an increase in consumer purchasing power.

b) Indirect benefits to UK consumers

7.49 Consumption and consumer welfare will likely increase because of EVFTA due to several reasons:

- As a result of the EVFTA, UK consumers will have a wider variety of choice in the goods and services they can consume, as Vietnamese goods will become less costly and easier to purchase. Prices may fall, and quality may increase.
- UK businesses will be able to import intermediate goods and services at a lower price due to EVFTA preferences. This allows the income of consumers to go further if firms pass lower import prices on to consumers in the form of lower goods prices.
- As UK firms face greater competition from Vietnamese firms, aggregate productivity may increase causing a subsequent increase in real wages.

  Baker and Vanzetti (2019) find that consumer welfare increases by £290 million per annum in the long run as a result of the EVFTA. These impacts are not captured in the total NPV as seen in section 9 as the welfare gains are an alternative way of looking at the impacts of GDP once accounting for price changes following the implementation of the EVFTA.

c) Direct cost to UK consumers

7.50 There are no direct costs on UK consumers.

d) Indirect costs to UK consumers

7.51 It is possible that in some sectors the exit of UK firms from domestic markets might reduce consumer choice.

Impact of EVFTA on the UK Exchequer

a) Direct benefits to the UK Exchequer

7.52 There are no direct benefits to the UK Exchequer.

b) Indirect benefits to the UK Exchequer

7.53 A loss in government revenue from reduced tariffs is in part a transfer to UK businesses who benefit from lower trade costs under the EVFTA preferences, and to consumers who will benefit from lower prices on final goods. The EVFTA is expected to increase domestic economic activity in specific sectors of the economy, which in turn will increase revenue for the UK Exchequer.

c) Direct costs to the UK Exchequer

7.54 The EVFTA is expected to increase domestic economic activity which will in turn increase revenue. This will be offset to some extent by forgone revenue to the EU and the UK from lower or eliminated tariffs on imports from Vietnam. To present the maximum loss of revenue of the EVFTA we assume that all tariffs are removed on entry into force. The UK exchequer could lose around £100 million from the elimination of all tariffs currently imposed on goods imported from Vietnam. Table 7 illustrates this in more detail below. It should be noted that that this is partly a transfer to UK consumers who may benefit from lower prices. This impact is not captured in the total NPV as seen in section 9 as it is implicitly captured within the impact on net UK GDP.

Table 7: Estimated foregone revenue in the UK from the reduction in tariffs

Top 5 Sector Name	Estimated annual revenue
Textiles and articles	£47 million
Footwear, headgear; feathers, artif. flowers, fans	£36 million
Prepared foodstuff, beverages, spirits, vinegar, tobacco	£7 million
Live animals and products	£5 million
Vehicles, aircraft and vessels	£5 million
Subtotal of Top 5 sectors	**£100 million**
Total of all sectors	**£104 million**

Source: Agriculture AVEs are sourced from the MacMaps, non-Agri AVEs are sourced from WITs World Bank and trade flow data is sourced from HMRC trade database. The estimated foregone revenue to the UK Exchequer from the elimination of tariffs imposed on Vietnam is based on average trade flow data from 2015 to 2017.

Notes: AVEs do not include the various reductions that importers can get, e.g. inward processing exemption, outward processing exemption.

Numbers may not sum due to rounding

d) Indirect costs to the UK Exchequer

7.55 There are no indirect costs to the UK Exchequer.

Assessment of policy option 2: UK does not support signature and conclusion of the EVFTA

7.56 Under this option the Government opposes the Commission's proposed decisions on signature and conclusion of the EVFTA. If the Council choose to use qualified majority voting and a qualified majority of Member States favoured proceeding to signature, the EVFTA would still come into force. Under this scenario, trading preferences set out in the EVFTA would apply to the UK and Vietnam and the associated gains would correspond to those set out under option 1.

7.57 Should the Council require agreement across the EU28 before proceeding, there is a risk that the agreement would not be implemented, meaning the EU and Vietnam would continue to trade on WTO MFN and GSP terms. Under this scenario, the UK would not accrue any additional costs and benefits and is therefore the same as under the baseline of this IA.

7.58 This is not the Government's preferred option, as it runs counter to the Government's policies in relation to free trade and its support for an ambitious EU trade policy. This could also damage the UK's bilateral relations with Vietnam and with the EU, which could make negotiations over future trading arrangements more challenging.

8 Small and micro business assessment

8.1 This section provides a qualitative impact assessment of the EVFTA on Small and Micro Businesses. It assesses whether the impact on the operations and performance of small businesses are likely to be disproportionate compared to larger businesses.

8.2 In 2016, there were 1,483 small and micro firms importing from Vietnam, and 1,609 small and micro firms exporting to Vietnam[29]. This reflects 57% and 56% of the total number of firms importing/exporting to/from Vietnam respectively. However, small and micro firms only represent 12% of import and 27% of export value. Comparatively, while large firms make up 14% of both importing and exporting firms, they account for 66% and 44% of import and export value respectively.

Rules of Origin

8.3 Small and micro firms in the UK will be able to choose to export goods and services under EVFTA preferences. These firms will have the incentive to export to Vietnam if the reduction in tariffs outweigh the cost of complying with rules of origin. If this cost is too high for small businesses, they can opt out and trade under the baseline MFN tariffs and as a result will not incur an additional cost above the baseline.

8.4 Cost will affect small business disproportionately to larger businesses as these firms will face relatively higher fixed costs compared to larger firms. Furthermore, small firms may not have the capacity and capabilities to deal with understanding the process and regulations around complying with Rules of Origin requirements compared to larger firms.

Tariff reductions

8.5 Small and micro firms in industries that are liberalised may expand production and experience an increase in revenue as their products become cheaper for Vietnamese importers. Similarly, small UK firms will be able to import products from Vietnam at a lower cost. This could lead to small businesses becoming more productive and competitive in the UK.

8.6 Some less competitive small businesses in the UK may be adversely affected by greater competition from Vietnam. However, the net impact on small businesses is expected to be positive.

[29] Values for the number of sole traders have been supressed by HMRC so are not included in the count.

Mutual recognition agreements

8.7 The burdens of understanding and addressing technical barriers to trade such as different conformity standards and regulatory requirements in Vietnam can be disproportionately large for small businesses. EVFTA provides a basis for the mutual recognition of certain standards, which could reduce the costs to business of conformity assessments such as product testing. This may be of particular benefit to small business exporters. In addition, small businesses in the UK might benefit if they can import products at a lower cost as a result of reduced product assessment costs in Vietnam.

9 Total Net Present Value impacts on the UK population under Option 1

9.1 Our estimate of EVFTA's net impact on UK GDP is £391 million relative to a baseline where the agreement is not implemented in the long run. The immediate gain in UK GDP is £474 million compared against a baseline where the agreement is not in force. This gain stabilises in the long run steady state to £391million. The gains decline in later years because of greater tariff reductions by 2030. Over time, greater tariff reductions across the EU and Vietnam are expected to result in negative terms of trade effects for the UK relative to Vietnam. In other words, in the long run, the price of UK imports from Vietnam are higher relative to the price of UK exports to Vietnam. Baker and Vanzetti (2019) find this result is driven by the relative price changes of motor vehicles, chemicals rubber and plastics, manufactured goods, air transport, financial services and other business services.

9.2 As shown in Table 8, below, in total the benefits to the UK are estimated to equal £6,350 million over a 15-year period. Costs are estimated at around £1.35 million over the same period. Subsequently, it is estimated that the net impact, in present value terms of option 1 is around £5,097 million over 15 years.

Table 8: The estimated total Net Present Value (NPV) of EVFTA across 15 years

Total Impacts on the UK (£m)	*Y1*	*Y2*	*Y3*	*Y4*	*Y5*	*Y6*	*Y7*	*Y8*	*Y9*	*Y10*	*Y11*	*Y12*	*Y13*	*Y14*	*Y15*	*Total*
Costs (2017 Real Prices)																
One-off familiarisation costs	0.81	0.34	0.20													1.35
Benefits (2017 Real Prices)																
Increase in UK GDP	474	467	460	453	446	439	429	420	410	400	391	391	391	391	391	6,350
Total NPV Costs	0.81	0.33	0.19													1.34
Total NPV Benefits	474	451	429	408	389	370	349	330	311	294	277	268	259	250	241	5,099
Total Business NPV	**473**	**451**	**429**	**408**	**389**	**370**	**349**	**330**	**311**	**294**	**277**	**268**	**259**	**250**	**241**	**5,097**

Note: The benefits are estimated to be £391 million in 2017 prices in the long run. This is discounted to calculate present value gains which is estimated at £241 million in appraisal year 15. We do not expect all firms to incur the one-off familiarisation costs in the first year of EVFTA's implementation. We assume that 60% of the total one-off familiarisation cost to businesses (£0.8 million) occurs in the first year that EVFTA is implemented, followed by 25% in year two and 15% in year three.

10 Sensitivities

10.1 This section explores the degree to which our understanding of the net benefits can change when considering the construction of a CGE model.

CGE modelling

10.2 CGE models are used widely to estimate the impact of trade policy changes. However, there are several limitations of these models. The results depend on the underlying assumptions and parameters that are used in the model, which to some extent are subjective and difficult to estimate – for example estimating elasticities in certain markets and regions. The results will also depend on the data used in the model and the assumption that future outcomes depend on past behaviour, which is not always the case. For example, if bilateral trade flows between two countries are non-existent or negligible, trade cost reductions facilitated by a trade agreement will not stimulate much impact in a CGE model.

10.3 However, CGE models can sometimes underestimate the full benefits of policy changes, as it is difficult and often requires further assumptions to model a comprehensive set of dynamic changes. For instance, this trade agreement is likely to result in increased competition between firms, which could result in higher levels of innovation. However, the positive impact of increasing innovation is not included explicitly within the model.

10.4 With regards to a change in trade policy there are two specific parameters built into CGE models that when altered have a substantial effect on the results: Firstly, the elasticity that describes how tariff changes impact trade flows. Secondly, the degree to which regulatory barriers between the EU and Vietnam converge.

10.5 Through the use of CGE modelling we can understand the how GDP, trade, welfare, domestic production can change from the implementation of a trade agreement. However, these results cannot be added without double counting benefits.

- **Real GDP** captures the impact of a trade agreement on the quantity of output an economy can produce in the long run. This does not take into account the impact of a trade agreement on the “terms of trade” – that is, on the relative price of a country’s exports relative to the price of its imports. In addition, it does not take into account the change in consumer prices.

- **Consumer welfare** is used to assess the impacts on consumers when prices fall due to trade liberalisation. This is measured using a method called “equivalent variation” which looks at how much consumers would need to be paid or compensated to keep them as well off in the absence of the trade agreement.

  Each of these can be calculated in a way that is consistent, but cannot be added without double counting benefits.

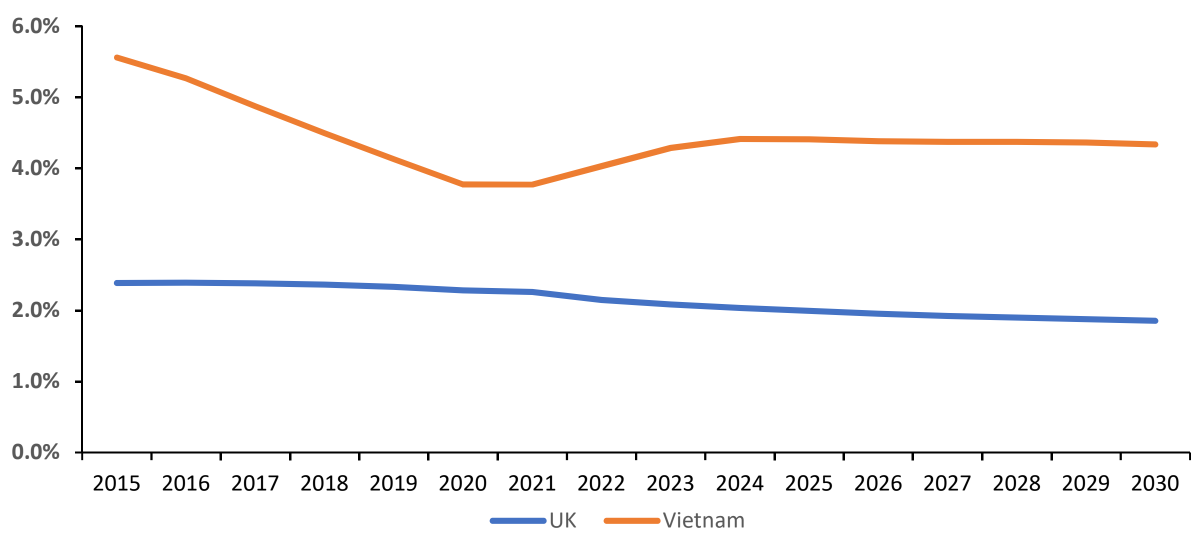
11 Risks and assumptions

11.1 The section below sets out the key modelling assumptions regarding the baseline, exchange rate, competition, employment and the UK's relationship with the EU.

11.2 **Baseline assumptions**: The baseline scenario in Baker and Vanzetti (2019) assumes no changes in trade policy - tariffs and NTMs remain as they are at present, subject to the conclusions of trade negotiations currently underway. The study projects the world economy to 2020, 2025 and 2030. The study's model runs on the GTAP database, version 10. This is a commonly used database and is seen to have the most update, internally consistent data on production, consumption and international trade by country and sector. The database for the model was benchmarked for 2014, then projected up to 2030 in real terms.

11.3 **Economic growth:** The analysis accounts for economic growth in the UK and Vietnam. GDP growth in the UK is estimated to be 2.3% in 2015 and declines to 1.9% in 2030. In comparison, Vietnam's GDP growth is estimated at 5.8% in 2015, takes a dip in 2020 and levels off at around 4.5% by 2030.

Graph 7: Year on year GDP growth assumed within the CGE analysis



Source: International Monetary Fund.

11.4 **The UK and the EU's relationship:** The future trading agreement between the UK and the EU is exogenous and for modelling purposes is assumed to be on the current status quo basis.

11.5 **Full employment:** The study assume a fixed amount of employment in the UK economy. This means workers based in sectors that contract following the implementation of the EVFTA move to more productive sectors of the economy.

11.6 **Market Structure:** The analysis that all firms have the same characteristics and sells the same type of products for the same price. There are no barriers to entry into the market meaning businesses can enter and leave the market with ease, making it a highly competitive market. In practice the structure of markets can vary by sector depending on the barriers to entry and ability for firms to ascertain a large market share. By assuming perfect competition, gains from an increase in productivity and innovation are not explicitly accounted for. Therefore the results presented in the impact assessment are towards the lower bound.

11.7 **Sector aggregation:** CGE models require an aggregation of sub sectors into larger groupings. This can obscure specific sector impacts as NTMs or tariff changes for sub sectors will be aggregated to a higher level.

11.8 **Rules of Origin**: For modelling purposes, the CGE analysis assumes full diagonal cumulation of EU content in UK exports to Vietnam.

11.9 **Service openness:** Baker and Vanzetti (2019) make expert judgements on the extent to which market access increases in service, using the Service Trade Restrictiveness Index (STRI). The baseline costs associated with trade in services between the UK and Vietnam are based on a study produced by the World Bank published in 2014.[30] The table below sets out the assumption used in the CGE modelling. The degree of service liberalisation is greater in Vietnam than in the EU. The communication and other transport sector are expected to open up the most in Vietnam under the EVFTA. In comparison, businesses services are assume to open up the most in the UK under the agreement. As mentioned in section 7, the estimates presented in table 9 reflect the authors' interpretation on the EVFTA text and their judgement of the additional market access offered under the agreement and is therefore subject to a degree of uncertainty. Overall, we expect the cost reduction presented in table 9 to be the upper end scale of the impacts.

Table 9: Degree of liberalisation in services

	UK exports to Vietnam (%)	Vietnamese exports to the UK (%)
Communication	75	2
Other transport	70	28
Sea transport	50	20
Retail & wholesale trade	50	6

[30] http://documents.worldbank.org/curated/en/137321468331910699/Estimates-of-ad-valorem-equivalents-of-barriers-against-foreign-suppliers-of-services-in-eleven-services-sectors-and-103-countries

Business services nec	25	48
Air transport	72	20
Finance & insurance	25	16
Recreation and other services	25	0
Other services	25	0
Source: Baker and Vanzetti (2019) Notes: The degree of liberalisation is bounded between 0 to 100, where 100 is complete opening of the sector.		

11.10 **NTMs of goods:** The EVFTA is expected to remove a limited number of NTMs. Some regulatory barriers to trade Regulatory changes will also occur across food products, beverages and chemicals. In general the EU is expected to make fewer regulatory adjustments.

11.11 The reduction of regulatory barriers to trade are often expressed as an Ad Valorem Equivalent (AVE) or tariff equivalent. However, Baker and Vanzetti (2019) express this in the form of a 'productivity shift'. In other words, a reduction in regulatory barriers is reflected as a reduction in production cost to businesses. It is important to note that the modelling does not capture the elimination of NTMs but models the impact of regulatory convergence. The authors source the baseline NTMs between the UK and Vietnam from the United Nations Conference on Trade and Development (UNCTAD) NTM database. A gravity model is used to assess the how much input prices change for businesses as a result of greater regulatory convergence between the EU and Vietnam.[31] The table below shows the reduction in production cost for businesses when trading under the EVFTA. For example, the production cost for UK export to Vietnam in beverages and tobacco and chemicals, rubber and plastics have reduced by 2% and 1.9% respectively. As mentioned in section 7, the estimates presented in table 10 reflect the authors' interpretation of the EVFTA text and their judgement on the additional market access offered under the agreement and is therefore subject to a degree of uncertainty.

Table 10: Reductions in domestic production cost by sector as a result of EVFTA		
	EU/UK exports to Vietnam	**Vietnam's exports to EU**
Rice	3.7	1.4
Sugar	2.8	1.2
Forestry	2.5	1.3
Food products nec	2.3	1.3
Dairy products	2.3	1.5
Fishing	2.2	1.2
Vegetables, fruit, nuts	2.2	1.5
Pork and poultry	2.1	1.4

[31] The database for Vietnam and other ASEAN countries is described in Ing et al (2016) and the methodology for calculating the price impacts is described in Cadot et al. (2015) and detailed further in Knebel and Peters (2018).

Beverages & tobacco	2.0	1.1
Other crops	1.9	0.7
Chemical, rubber & plastics	1.9	0.7
Beef and veal	1.7	1.4
Petroleum, coal products	1.4	0.7
Textiles	1.4	0.6
Resources	1.3	0.5
Leather	1.2	0.6
Wood products	1.2	0.7
Motor vehicle & trans equip	1.0	0.6
Ferrous metals	0.9	0.3
Mineral products nec	0.7	0.3
Manufactures	0.7	0.3
Minerals	0.5	0.4
Wearing apparel	0.4	0.7
Paper products, publishing	0.3	0.3
Machinery and equipment nec	0.1	0.3
Electronics	0.0	0.2
Source: Baker and Vanzetti (2019)		

11.12 **Exchange rate:** The original data from the GTAP model are in US dollars at 2014 prices. We can estimate the equivalent pound sterling in 2017 prices by first inflating US dollar prices from 2014 to 2017 and then converting to pound sterling by estimating a 2017 exchange rate of 1.31 £/USD based on data from the International Monetary Fund (IMF).

Annex A: Explanation of CGE modelling

There are various well established robust methods to estimate the impact of trade agreements namely:

- **Econometric gravity modelling** – This type of modelling predicts bilateral trade flows based on the economic size of the countries in question and their geographic distance. Expansions of gravity modelling have included other components of 'distance' including trade costs and other country characteristics such as culture and language. This method has been applied since the late 1960's and is predicated on historical data.
- **Partial equilibrium modelling** – This tool of analysis estimates the isolated impact of a change in policy in one sector, e.g. automotive, agriculture, financial. In the context of trade agreements, it looks at the impacts of changes in trade costs on a sector's production, exports, and imports. While it can observe the impacts for a much more granular sectoral aggregation that CGE models, it does not capture positive or negative spillover effects on complementary sectors or the wider economy.
- **General equilibrium modelling** – This model links all sectors and agents of an economy together and therefore captures any positive or negative spillover effects from a trade agreement. For example, if tariffs are reduced for a particular good, its use as a final and intermediate good may increase due to lower prices. This has expansionary effects for other sectors that rely on the good for their own production and further knock-on effects for the incomes of workers, firms, and government.

Annex B: The impact of future free trade agreements on the baseline

The European Commission's study was concluded in 2013. The elimination of tariffs sets out in CPTPP is included in the baseline analysis. However liberalisation associated with regulatory barriers to trade are not factored in. Modelling that captures the impact of the EU-Vietnam free trade agreement on the UK specifically, taking into account all the final provisions set out in CPTPP, is not available.

CPTPP will bring the harmonisation of certain standards and reductions in NTMs that will affect the flow of both goods and services between CPTPP members and could lead to diversionary effects. We do, however, expect the negative impact of CPTPP to be small in the short term, because Vietnam already has FTAs in force with 7 out of the 10 other CPTPP members (excluding Vietnam itself). Vietnam does not currently have FTAs with Canada, Mexico and Peru.

The main goods exported by UK businesses to Vietnam differ from those exported by Canada, Mexico and Peru. Firstly, the top exports to Vietnam by Canada are cereals, fish and crustaceans, and oils and seeds. Secondly, for Mexico, the top exports are aluminium, fish and crustaceans, and fruit and nuts. Thirdly, for Peru the top exports are ores, slag and ash, and meat products. However the top UK exports to Vietnam are nuclear machinery and mechanical appliances, pharmaceutical products, electrical machinery and equipment.[32] As the majority of the products are different, diversionary effects on goods trade are likely to be minimal.

Data is not readily available on service trade between the UK, Mexico, Canada, and Peru with Vietnam by service sector so we cannot compare exports in detail. However, we would expect the impact of trade diversion on services to be minimal. In 2016, 16% of Canadian exports to Vietnam were in services whereas in 2017, 33% of UK exports to Vietnam were in services.[33,34] As Canada's share of service exports is much lower than the UK's, we would expect CPTPP to lead to minimal trade diversion in services. Similar data was not available for Peru and Mexico.

Annex C: Factors affecting GDP

GDP is the summation of aggregate consumption, investment, government expenditure, and net trade (exports – imports). As presented in the main body of the impact assessment, Baker and Vanzetti (2019) estimate the EVFTA could result in a £490 million increase in UK exports to Vietnam, a £1.7 billion increase in UK imports from Vietnam, and a £390 million increase in UK net GDP.

Although not explicitly stated in Baker and Vanzetti's results, the impact of a trade agreement also affects other components of GDP. One of the advantages of the CGE model used is that it captures links between markets throughout the economy so that the wider effects can be captured, rather than a narrow focus

[32] Product data from UNCOMTRADE, 3 year average (2015-17)

[33] Global Affairs Canada Trade Statistics

[34] ONS Balance of Payments

on imports and exports. This is why the impact to GDP is positive even though the trade balance has declined.

An FTA can allow for UK businesses and consumers to import intermediate and final goods at a lower cost. This lower cost could also be passed onto consumers in the form of lower prices, inducing increased consumption. Cheaper intermediate products could also increase UK businesses profitability, extra profits can then be used for either increased domestic investment or higher wages and tax receipts, hence providing a potential boost to government expenditure and consumption.

Other examples include Copenhagen Economics assessment of EU-Japan Economic Partnership Agreement (2009). Gains in EU imports are estimated at €35.3 to €53.8 billion, whereas export gains are only €27.8 to €43.3 billion. However, the overall impact on EU GDP is positive equal to increase of between 0.10% to 0.14%.

Annex D: Method description: estimated one-off costs associated with EVFTA text familiarisation costs

The steps below set out the method applied to estimate the one-off familiarisation costs to businesses.

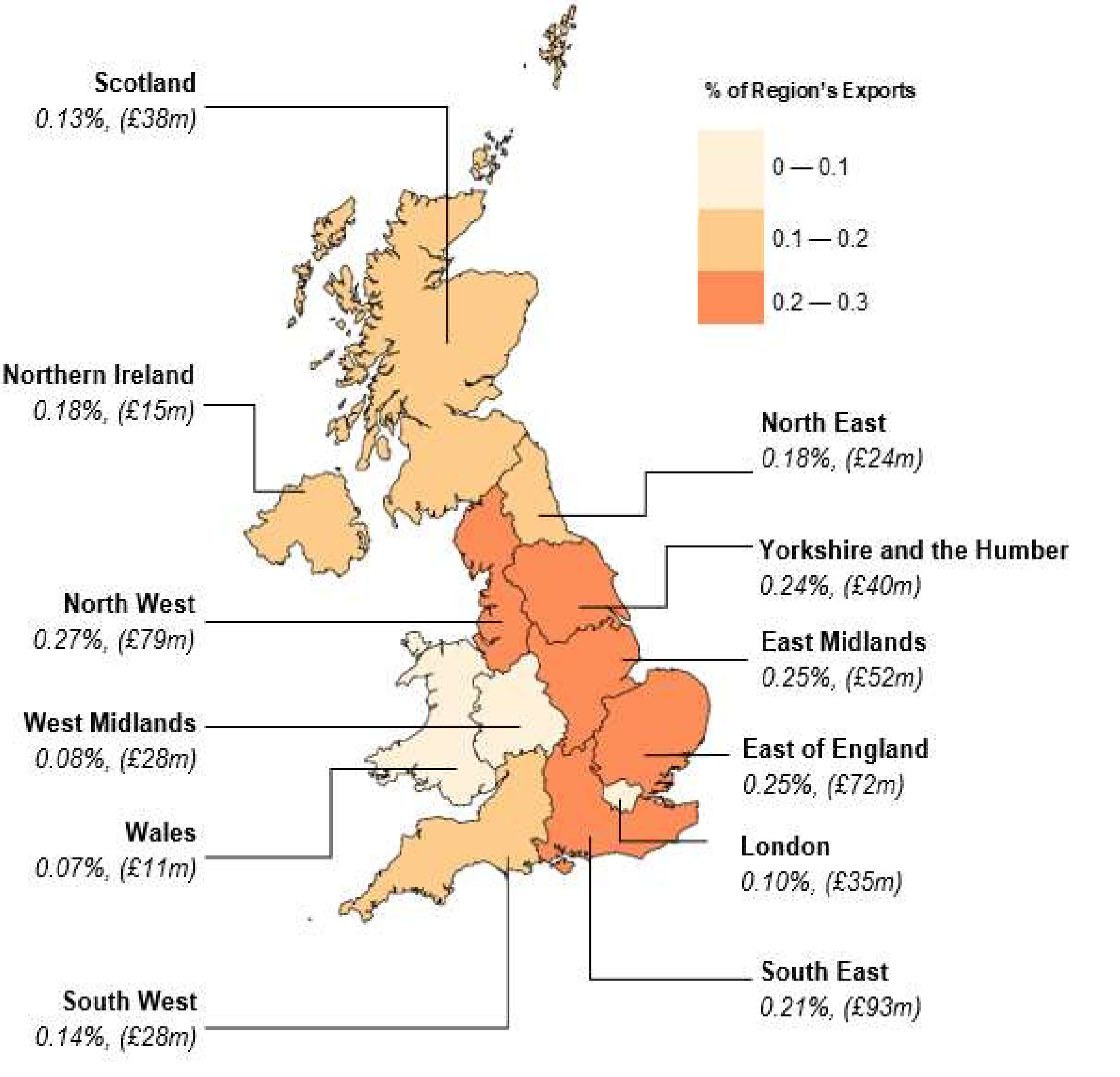
1	We assume that 40% of UK businesses that trade with Vietnam will read the full agreement, this includes: • 18 chapters and 17 annexes of the EU-Vietnam Free Trade Agreement text[1], authentic as of January 2016. We assume a business will read the document stated above which collectively total 192,268 words.
2	Evidence shows the average reading time is 228 words per minute with a range of 30 words either side.[2]
3	Based on the information above, we estimate the following ranges of time it may take a firm to become familiar with the EVFTA text: a) High scenario: assuming an employee reads 198 words per minute, it will take 16.2 hours to read the document above. b) Central scenario: assuming an employee reads 228 words per minute, it will take 14.0 hours read the collective documents above. c) Low scenario: assuming an employee reads 258 words per minute, it will take 12.4 hours to read the collective documents.
4	Average weekly earnings are £472 from the year ending September 2017 and the average number of hours worked per week is 37.5 over the same period. From this we estimate the average hourly pay is £13 per hour. [3]
5	We uplift this by 20.2% to account for other non-wage labour costs such as national insurance, pensions and other costs that vary with hours worked, revising the cost per business to £15.63 (£13 + £2.62).[4]
6	The cost for one business to read the EVFTA text and guidance is estimated at: a) High scenario: £252.89 (£15.63 x 16.2 reading hours)

	b) Central scenario: £219.62 (£15.63 x 14.0 reading hours) c) Low scenario: £194.08 (£15.63 x 12.4 reading hours)
7	Published data shows 2,874 UK businesses exporting to Vietnam and 2,611 importing from Vietnam in 2016.[6] The total number of firms trading with Vietnam is therefore 5,485. The 40% of firms (2,194) which choose to read the full agreement incur some familiarisation costs: a) High scenario: £554,849 [(2,194 x £252.89 cost per firm) b) Central scenario: £481,843 [(2,194 x £219.62 cost per firm) c) Low scenario: £425,815 [(2,194 x £194.08 cost per firm)
8	Alternatively, businesses may seek advice from a specialist agent on interpreting the text and implications for their trade. Survey evidence shows that 60% of businesses seek advice from an agent to complete tax affairs. Using this as a proxy for the number of firms which would seek advice on EVFTA. The same survey provides an average cost of using an agent of £265.[5]
9	Published data shows 2,874 UK businesses exporting to Vietnam and 2,611 importing from Vietnam in 2016.[6] The total number of firms trading with Vietnam is therefore 5,485. The 60% of firms (3,291) that choose to seek advice from an agent will incur the following costs: • £872,115 (3,291 firms x £265 cost per firm)
10	We assume that 100% of firms use the EUSFTA preferences and therefore incur some familiarisation costs: d) High scenario: £1.43 million (£554,849 + £872,115) e) Central scenario: £1.35 million : (£481,843 + £872,115) f) Low scenario: £1.30 million (£425,815 + £872,115)
Sources : [1] http://trade.ec.europa.eu/doclib/press/index.cfm?id=961 [2]http ://iovs.arvojournals.org/article.aspx? articleid=2166061#90715174 [3] Labour market statistics summary data tables (ONS) 2017. Table 15. Average Weekly Earnings (nominal) – Regular Pay (Great Britain, seasonally adjusted). [4] Understanding tax administration for businesses, HM Revenue and Customs Research Report 375, July 2015 https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/443746/HMRC_Report_375_Tax_Administration.pdf https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/employmentandemployeetypes/bulletins/uklabourmarket/october2017/relateddata [5] As cited in the Green Book, HSE uses 30% as an adjustment for non-wage labour cost. This is based on the labour force survey 1992. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/220541/green_book_complete.pdf [6] IDBR overseas trade statistics country data tables 2016. https://www.gov.uk/government/statistics/uk-trade-in-goods-by-business-characteristics-2016.	

Annex E: Distribution impacts

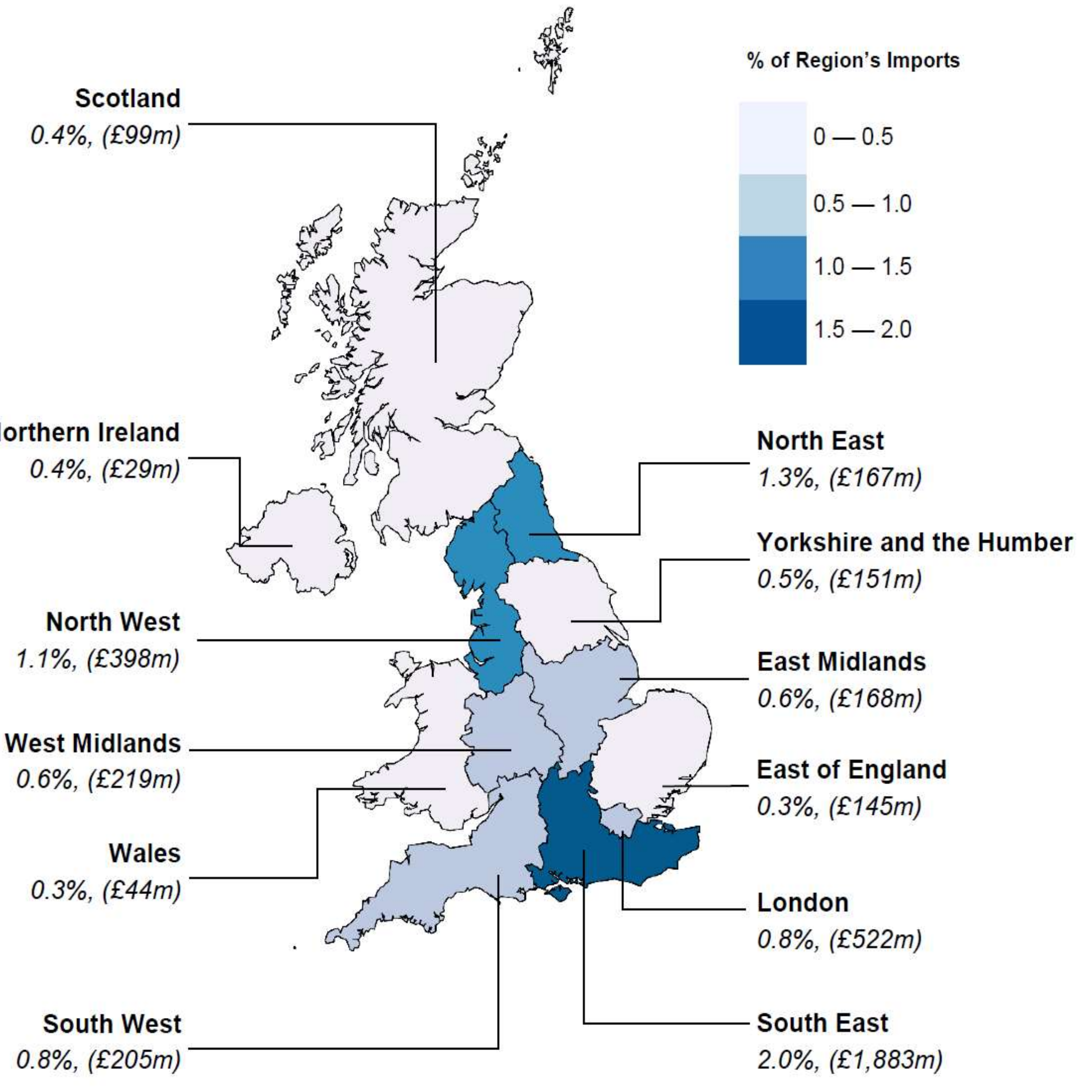
Section 7 showed that, under EVFTA, UK exports to Vietnam could increase by £490 million and UK imports from Vietnam could increase by £1.7 billion in the long run. The evidence indicates that most of the export gains will be in the finance and insurance sector and most of the import gains will be in the wearing apparel, leather products and motor vehicle and transport parts. The graphs below highlights UK exports to Vietnam are mostly concentrated in the North West in 2017 relative to the rest of the UK. In comparison, the data shows UK imports from Vietnam are mostly concentrated in the North East in 2017.

Graph 8: UK exports of goods to Vietnam by area in 2017



Source: HMRC, Regional Trade Statistics
Note: The percentage shares represent the value of trade each area exports in goods to Vietnam compared to the value of trade each area exports to the world.

Graph 9: UK imports of goods from Vietnam by area in 2017



Source: HMRC, Regional Trade Statistics
Note: The percentage shares represent the value of trade each area imported in goods from Vietnam compared to the value of trade each area imported from the world.