



Asian Productivity Organization “The APO in the News”

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Low labour costs won't serve Vietnam's development indefinitely.

Since China faced a decline in its role in manufacturing, Vietnam has become an emerging market for investors. Over the last decade the country's processing and manufacturing sector has attracted thousands of foreign direct investment (FDI) projects thanks to its cheap labour and infrastructure costs. Trade has increased three-fold since 2007, reaching \$350.7 billion, according to the general Department of Vietnam Customs. The country's abundant, cheap labour has played an increasingly pivotal role in wooing foreign investors looking to set up overseas manufacturing operations.

Competitive advantage

Vietnam's low labour costs have transformed the country into a key Asian electronics manufacturing hub and lured production away from China. At 6.3 per cent of GDP, it has attracted more than five times the FDI going to China or India over the last five years. Huge investments are anticipated over the coming decade in next-generation manufacturing across a wide range of industries. Labour costs are considered a decisive competitive advantage, followed by the tremendous opportunities from market reforms to unlock potential and drive the industry forward.

A recent report from the Japan External Trade Organisation (JETRO) showed that abundant and low-cost labour ranks in the Top 5 advantages in Vietnam's business climate, as identified by 54.1 of the Japanese enterprises in Vietnam surveyed. "Vietnamese are viewed as hard working and dedicated," Atsusuke Kawada, Chief Representative of JETRO in Hanoi, said. "While Japan's workforce is aging, Vietnam population structure is in a golden era."

Vietnam's abundant and low-cost labour, according to Phan Thanh Xuan, general Secretary of the Vietnam Leather, Footwear and Handbag Association (Lefaso), has been behind the large number of foreign-invested enterprises (FIEs) entering its processing and manufacturing sector over the last 20 years. China, meanwhile, has seen incomes rise in the sector and cut incentives to FIEs in recent years, which encouraged investors to shift their factories to Vietnam.

Textiles and garments have also benefited from abundant, cheap labour. The sector is Vietnam's largest industrial employer, with more than 2.5 million workers, accounting for 25 per cent of the total workforce in the industrial sector and generating 17 per cent of Vietnam's export revenue (\$27.2 billion in 2015), according to the Vietnam National Textile and Garment Group (Vinatex). The industry specialises in the lowest value-added segment in the middle of the global supply chain. Workers from rural areas are trained to specialise in cutting, trimming and making garments, which accounts for 78 per cent of textile and garment exports.

Labour productivity remains the dominant element in the development of the textile industry, according to Le Tien Truong, CEO of Vinatex. A value chain in the textile and garment industry starts with creating fabric, cutting and sewing, then moves on to distribution of final products. "At present, 85 per cent of Vietnamese enterprises focus on cutting and sewing, which are labour-intensive," he said. "To meet growing demand for textile products from other markets in free trade agreements, the only way is to increase labour productivity, because a worker cannot operate two sewing machines simultaneously."

Vietnam has made remarkable progress in its gender equality initiatives, which is crucial to the expansion of the country's workforce and improving labour productivity – two imperatives needed for its economy to sustain steady growth as its manufacturing industry develops. Samsung's recruitment strategy looks to take advantage of this trend and it predominantly employs female factory workers.

Though Samsung constitutes the largest FDI in Vietnam, recently increasing this by around 40 per cent to \$12 billion, the company is not the only high-tech company operating in the country. Panasonic, a leading Japanese electronics manufacturer with over 8,000 employees, found that it is necessary to develop the strengths of its workers. "Vietnamese are hardworking, intelligent and creative," said Mitsuhiro Takayanagi, director of Human Resources and general Affairs, Panasonic Vietnam. "Panasonic very much focuses on establishing research and development centers and creative new products that need talented employees. We have therefore conducted a lot of training in soft skills and technical skills to have a well-trained workforce."

Challenges to come

Productivity in Vietnam has indeed risen in the last decade, starting at \$1,081 per person in 2005 and reaching \$3,551 in 2015, according to data from the Asian Productivity Organisation in 2015. Compared to other Asian countries, however, this increase is not significant and the country's productivity is still below the regional average. Vietnam ranked 52nd in the overall labour market efficiency rankings, 85th in labour market flexibility, and 42nd in efficient use of talent, according to the Global Competitiveness Report 2015-2016 compiled by the World Economic Forum.

The JETRO report shows that 60 per cent of Japanese enterprises in Vietnam view rising labour costs as a challenge. "Vietnam may lose its competitive edge in the manufacturing sector," Kawada said. "One of the challenges is rising wages, while productivity still lags behind."

It's clear that low labour costs will not remain an advantage for Vietnam in the years to come. A young, inexpensive workforce was the country's biggest advantage in the initial stages of its economic development. "Now, Vietnam has integrated more deeply into the global economy while adapting to the fourth revolution in science and technology," Vu Tien Loc, Chair of the Vietnam Chamber of Commerce and Industry (VCCI), told VET. "A creative workforce is the biggest advantage nowadays, not a low-cost, low-skilled workforce as in the past."

Moreover, Vietnam's labour market is and will be impacted more strongly by the development of technology. Eighty-six per cent of wage workers in the textiles, clothing, and footwear sector are at high risk from automation, according to the 2016 Asean in Transformation report from the International Labour Organisation (ILO). The country will increasingly witness the impact of technological change in the workplace. "Technology increases the number of operational choices available to enterprises, allowing investment decisions to be made based on a multitude of factors," the report noted. "Multi-national corporations are less likely to base their production and investment decisions principally on low labour costs."

"Some innovations, such as robotic automation, are already penetrating into different industries such as garments and textiles and electronic and electrical products," said Miranda Kwong, Labour Economist at the ILO in Vietnam. "In the future, these two sectors will likely be impacted by technological transformation, and skills and workforce readiness will be critical issues for Vietnam."

Believing that automation is not a fatal challenge for the footwear industry, Xuan from Lefaso said that many production stages in the industry will always require human input. "Automation should have a roadmap, as the sector still requires skilled workers with high technical qualifications," she said. "Fashion products are constantly changing, so speed is always necessary, which needs a combination of people and machinery. Many foreign enterprises in the footwear industry are gradually upgrading their production lines and improving their workers' skills."

As a representative of enterprises, Loc said that Vietnam needs to reform its vocational training system, which is a key element in the course of restructuring the national economy. This requires the development of a comprehensive strategy. "Job training nowadays should be shared between the government and the private sector, particularly in the field of high skills training," he said.

Fifty per cent of enterprises haven't anticipated what skills will be needed in the future and 38 per cent don't have close links with vocational schools or other training facilities, according to a survey by the Institute of Labour Science and Social Affairs. Close cooperation between policymakers, employers and training institutions to modernise the skills development system to better anticipate changing workplace dynamics and new technological innovations is crucial, Kwong said. Promoting both academic education in the fields of science, technology, engineering and mathematics is important, along with developing strong core skills such as communications, teamwork and creative and analytical thinking, particularly among young women.