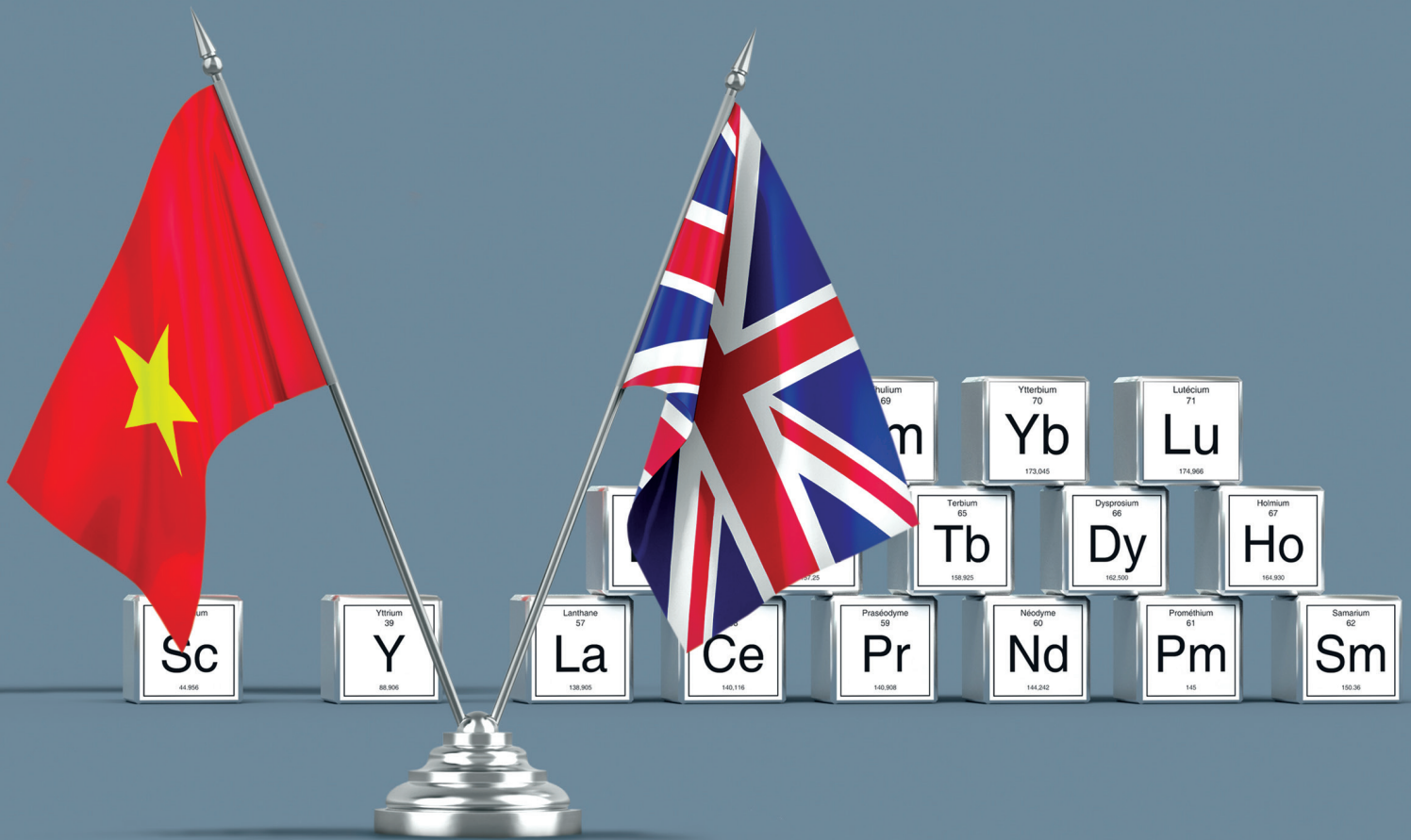


Rare Earths: A case for closer trading relations between the UK and Vietnam

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Executive Summary

This paper sets out to explore the importance of the UK-Vietnam trade corridor and the reasons for focusing on deepening the Free Trade Agreement that exists between the two countries. In the current context, where China is seen by the UK government as an 'epoch-defining challenge'¹ there are clear reasons for working with other powers in the region to reduce the UK's supply chain dependencies on China. In the rare earth metal space, deepening the relationship between the UK and Vietnam would allow supply chain resilience to be enhanced for one party and investment opportunities to be realised for the other.

Introduction: The current trading relationship

Vietnam's economic growth was nearly 6% in 2022 according to Trading Economics.² Bilateral trade in goods and services between UK and Vietnam was worth some £6.4bn in the four quarters to the end of Q3 2022, with UK exports to Vietnam at around £950m and UK imports from Vietnam of around £5.4bn. This represents an increase of 13.6% for exports and 21.8% for imports over the previous year.³ PwC describes Vietnam as a "Rising Dragon"⁴ with a large market given the size of its population of over 98 million people, a favourable business environment and free trade agreements with partners who are important to the UK, including the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) and the EU-Vietnam Free Trade Agreement.

Strategic potential for both countries

All of this makes Vietnam a key strategic partner for the UK to complement trading relationship with China. Trade with Vietnam is a fraction of UK trade with China⁵: Vietnam is the UK's 41st largest export partner while China is its 7th⁶; Vietnam is the UK's 24th largest import partner while China is its 1st. However, Vietnam's importance to the UK cannot be understated: as a member of the CPTPP it is essential to approving the UK's own membership application; as a member of ASEAN it has a role in furthering UK interests in the Indo-Pacific; and as a major producer and exporter of rare earth metal ores, it has a substantial role to play in supporting the UK's Supply Chain Resilience (SCR).

For Vietnam the benefits of deepening its relationship with the UK, beyond access to new markets and increasing its exports to the UK, are similarly strategic. The relationship between the two countries is good, and in growing closer to the UK, it can reduce its own reliance on China. A means of doing this may be through greater investment flows between the two countries. In 2021, the outward stock of Foreign Direct Investment (FDI) from the UK to Vietnam was £785m while the inward stock from Vietnam to the UK was £21m.⁷ This is an asymmetric relationship at present and declined between 2021 and 2022. This paper concludes by looking at how this relationship might be developed through closer relations between the two countries.

¹ Cabinet Office, (2023), *Integrated Review Refresh 2023: Responding to a more contested and volatile world*, Retrieved from: <https://www.gov.uk/government/news/pm-announces-major-defence-investment-in-launch-of-integrated-review-refresh>

² Trading Economics (2023), *Vietnam*, Retrieved from: <https://tradingeconomics.com/vietnam/indicators>

³ Department for Business and Trade (2023, February 17), *Trade and Investment Factsheets – Vietnam*, Retrieved from: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1136425/vietnam-trade-and-investment-factsheet-2023-02-17.pdf

⁴ PricewaterhouseCoopers (2021), *Vietnam: The Rising Dragon*, Retrieved from: <https://www.pwc.com/gx/en/services/consulting/strategy/vietnam-rising-dragon.html>

⁵ Department for Business and Trade (2023), *Trade and Investment Factsheets – Vietnam*, Retrieved from: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1136425/vietnam-trade-and-investment-factsheet-2023-02-17.pdf

⁶ United Nations (2023), *UN Comtrade Database*, Retrieved from: <https://comtradeplus.un.org/>

⁷ Department for Business and Trade (2023, February 17), *ibid.*

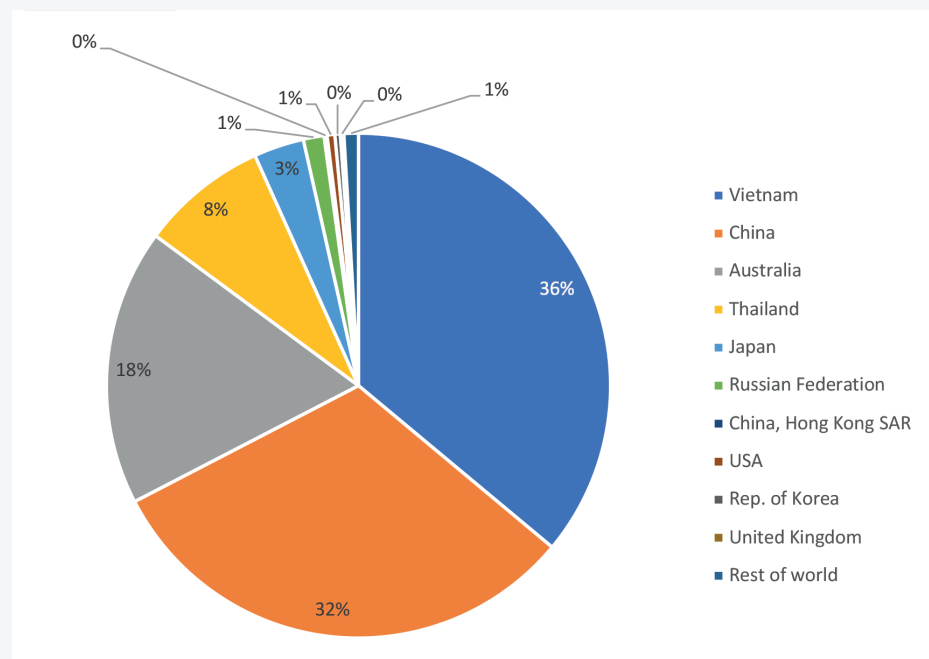
Resilience: Why rare earth metals matter to the UK-Vietnam trade partnership

Vietnam is the world's largest exporter of Rare Earth Elements (REE) in the form of ores – specifically monazite, Xenotime and bastnaesite. These are used variously in renewables and construction: Monazite is used in wind turbines, xenotime contains yttrium which strengthens alloys and is used in radars and laser applications, while bastnaesite contains cerium which is used in magnets and high tech communications. All three ores have multiple applications across the energy transition, net zero and supply chain resilience areas of national security.

As Figure 1 shows, Vietnam controls approximately 36% of world REE exports in 2021. However, because the exports are as ore rather than refined products, this makes the country dependent on others for the processing of ore into rare earths that can be used in production. While it accounts for such a sizable proportion of exports, its production was barely 400 metric tonnes in 2021.⁸

At present there is significant inward investment going into Vietnam from Australia for rare earth processing. Vietnam's attractiveness has increased as the country and its allies have shifted to a "China Plus One" strategy and since the Chinese dispute with Japan over the Senkaku islands. The result of the latter in 2010 was that China suspended the supply of REE elements to Japan, causing prices to rise significantly. Japan also has a strong partnership with Vietnam for investment in REE production but this has yet to convert into high levels of processing. However, because Australia has strong expertise in mining and production already, there are synergies between the two countries that it is well-placed to develop.

Figure 1 Share of world exports of Rare Earths, 2021



Source: Mirrored Comtrade data 2022 (author's own calculations)

⁸ Basan, N. (2022, November 21), *An Australia-Vietnam partnership could erode China's monopoly on rare earths*, *The Diplomat*, Retrieved from: <https://thediplomat.com/2022/11/an-australia-vietnam-partnership-could-erode-chinas-monopoly-on-rare-earth/>

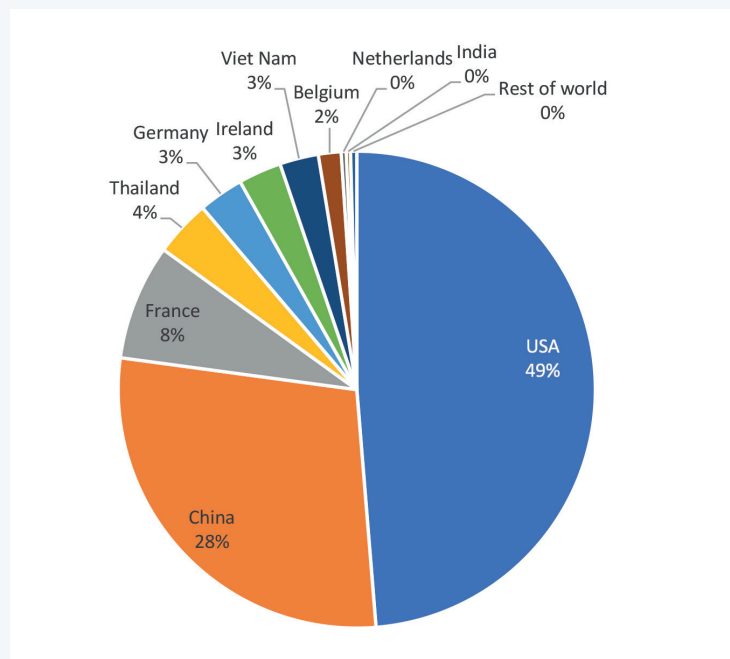
REEs are not in fact scarce, but they are precious because of the costs of extraction from ore.⁹ The UK has significant technological and financial advantages that could support Vietnam's embryonic production capabilities in a complementary way. Clean technology is a clear source of emerging technological and financial competitive advantage: the UK's Integrated Review, and its subsequent Refresh, highlight the importance of sustainability as a key driver of national security and the UK was among the first economies to make a legal commitment to net zero. In total, including public and private sector investments, the UK is set to increase its investments from an estimated £10-£15bn to over £50bn in order to reach these targets by £2050. In addition to this, the UK government is committed to a rare earth metals strategy to improve its supply chain resilience and it has a strong legal infrastructure which underpins both global trade and trade in commodities and is a pioneer in emerging legal frameworks for digital transferrable instruments. This provides both a framework for investment in REE supply chains that is world class and unrivalled, and a trade finance infrastructure that is efficient and effective.

Combining these factors with the innovation in the UK's globally leading universities and research-base with this financial strength gives it a unique competitive advantage. Its own base and rare earth metals industry is developing through its export infrastructure: the UK is the 12th largest exporter of Lithium in the world, for example. Since Vietnam's production of REEs uses outdated technologies and is mainly manual – if it is to become a competitor to China in this space, then it will need investment from many countries and the UK is well placed to provide both the technological expertise and the financial backing that its development will require.

From a British perspective, this is important in the context of the Refresh of the Integrated Review, which focuses heavily on the UK's need to invest more in resilience, and commits to “proactively support(ing) the capabilities, supply chains and technologies that are of strategic importance to the UK and the wider world.”¹⁰ In geoeconomics terms this means reducing

Figure 2 Share of UK REE imports 2021 (%)

BFPG



Source: Comtrade 2023

⁹ Teufel Dreyer, J. (2020, October 7), China's Monopoly on Rare Earth Elements – and Why We Should Care. Foreign Policy Research Institute, Retrieved from: <https://www.fpri.org/article/2020/10/chinas-monopoly-on-rare-earth-elements-and-why-we-should-care/>

¹⁰ Cabinet Office (2023, March 13), *Integrated Review Refresh 2023: Responding to a more contested and volatile world*, Retrieved from: <https://www.gov.uk/government/publications/integrated-review-refresh-2023-responding-to-a-more-contested-and-volatile-world>

dependency on China for critical supply chain components and extending our trade relations post-Brexit beyond the EU. REEs are critical to supply chain resilience but at present, reducing the UK's dependence on China will involve substantial investment in alternative processing and production capability. Vietnam is an ideal partner with which to develop this type of capability.

Understanding the REE trade corridor between Vietnam and the rest of the world is complex because the country only reports imports, which predominantly come from China. Figure 1 shows the mirrored data, that is, the average of the bilateral flow between each country, to derive the figures for exports. In the case of the UK, some \$21.2m of rare earth metals were imported in 2021, of which 2.6% came from Vietnam, making it the UK's 7th largest importer as illustrated in Figure 2.

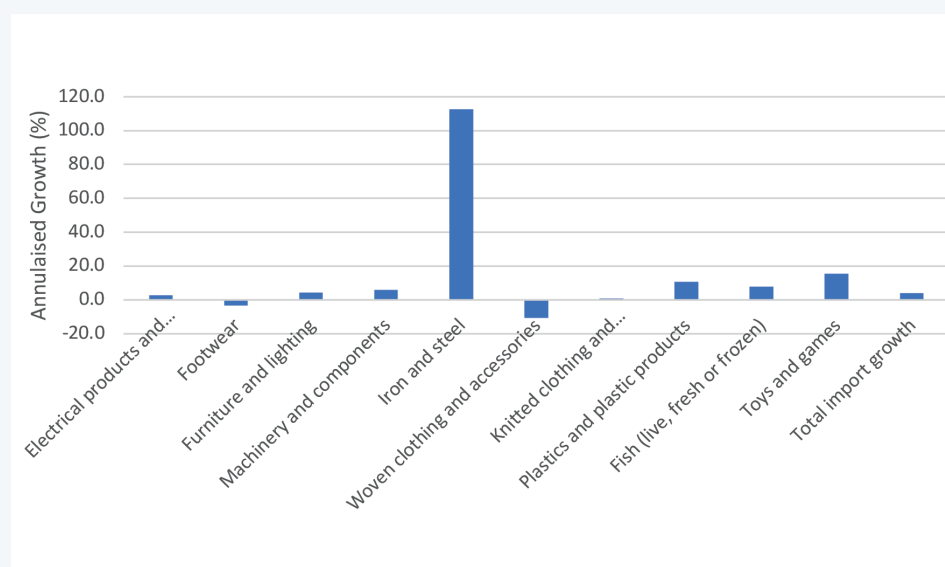
What is interesting about Figure 2 is that it suggests that 62% of UK supplies of REEs are from NATO countries. The US dominates, and France, Germany, Belgium and the Netherlands. However, a significant proportion of REEs comes from China at 28% of all imports.

Arguably it is here that the trade partnership with CPTPP generally and Vietnam in particular could make a genuine difference to UK security and supply chain resilience. This will undoubtedly take substantial outward investment from the UK to Vietnam and the transition from ore production to processing in Vietnam will take time to develop as well. However, the significance of the relationship in creating greater resilience is important and, in trade policy terms, should be prioritised.

Conclusion: A strategic opportunity to strengthen the relationship

Vietnam and the UK have had a strategic partnership since 2010 covering a range of foreign policy and economic, trade and investment areas as well as education, research and development and security policy.¹¹ Vietnam's access to the CPTPP and to the ASEAN region represents a substantial market opportunity for both the UK and Vietnam working together. The UK-Vietnam corridor is driven by high-end products such as electronics, pharmaceuticals and machinery and components. UK inward investment deals represent some 438 projects amounting to nearly \$4 billion in capital in Vietnam.¹² There are preferential investment terms for investment by UK companies in medical care including dental and hospital services as well as architecture, planning, engineering, education and the environment.¹³ This mirrors important and export trade in similar goods sectors as illustrated in Figures 3 and 4.

Figure 3 Top ten UK import sectors from Vietnam, CAGR 2016-2021 (%)



Source: Comtrade and Analytics Engines, 2022

Electronics is significantly larger than any other sector at some \$2.4bn. This reflects growing supply chains in computer components and semi-conductors. Interestingly, growth in machinery and components including computers, and iron and steel suggest that there may have been a more strategic focus on shifting supply chains away from China dependency over the last five years.

Over the past five years total UK exports to Vietnam have fallen slightly annually by -0.2% while pharmaceutical and electronics exports have also declined. There is still growth annually in medical equipment and wood pulp, and shipping exports have increased significantly. This may suggest that the UK is supporting Vietnam's trade infrastructure through increased exports of shipping.

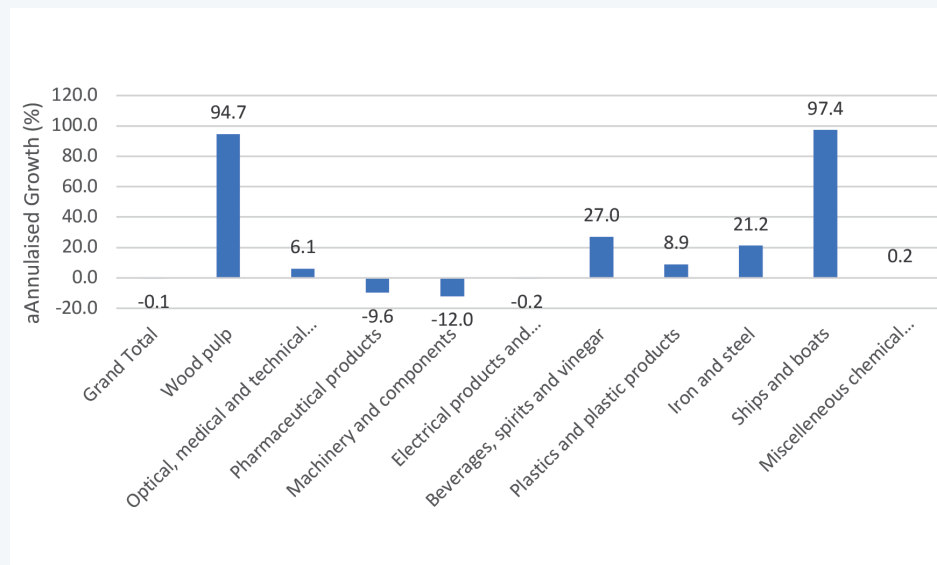
¹¹ Baker, P., Le, L., and Elder, A. (2023, February 28), *United Kingdom: UK's Trade under the UK-Vietnam FTA*, International Economics. Retrieved from: <https://www.tradeeconomics.com/united-kingdom-uks-trade-under-the-uk-vietnam-fta/>

¹² Vietnam Plus, (2022, August 18): *More British Investors look at Vietnam to cash in on free trade agreements*, Retrieved from: <https://en.vietnamplus.vn/more-british-investors-look-at-vietnam-to-cash-in-on-free-trade-agreements/235827.vnp>

¹³ Baker, P., Le, L., and Elder, A. (2023, February 28), *ibid.*

Figure 4 Top ten UK export sectors to Vietnam, CAGR 2016-2021 (%)

BFIG



Source, Comtrade and Analytics Engines 2022

Rare earth metals are strategically important for both countries but barely feature in the data. As the 2020 renewed Strategic Partnership document stresses the importance of common security interests in the Indo Pacific, it makes sense for the trade and investment collaboration between the two countries to include infrastructure investment in Vietnam’s emerging rare earth metals processing sector. This is where the UK can arguably help Vietnam to build its capabilities and competitiveness with China and it is also the arena where Vietnam can take a big lead alongside Australia and Japan within the CPTPP.

The picture on general trade between the two countries is mixed and it is important that the economic opportunities are not lost given the increased and likely enduring focus on strategic competition with China.¹⁴ There are shared interests and benefits in enhancing strategic trade relations in medicines and pharmaceuticals as well as in electronics, while the need for a combined approach to sustainability and reducing carbon emissions can be the focus of collaborative efforts between the two countries and across the CPTPP and ASEAN. Increased wood pulp trade may reflect opportunities to support recycling between the two countries, for example. What is absolutely clear is that by strengthening trade and strategic ties between the two countries, there is an opportunity to realise this potential to mutual advantage.

¹⁴ Hemmings, J. and Hayton, B. (2021, October), *Enhancing British-Vietnamese relations in a more competitive era*, Council on Geostrategy, Retrieved from: <https://www.geostrategy.org.uk/research/enhancing-british-vietnamese-relations-in-a-more-competitive-era/>

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