

Risk Management Readiness of Vietnamese SMEs under the Eu- German Supply Chain Due Diligence Act

Tran Duc Thang¹, Nguyen Thi Hong Nhung²

Abstract

The implementation of the German Supply Chain Due Diligence Act and the European Union's Corporate Sustainability Due Diligence Directive has significant implications for the Vietnamese small and medium-sized enterprises (SMEs) integrated into global supply chains. This study assesses the readiness of the Vietnamese SMEs in adopting risk management practices to comply with these regulations. Utilizing a mixed-methods approach, the study reveals limited awareness and implementation of due diligence requirements among the SMEs, highlighting the need for targeted support and capacity-building initiatives.

Keywords: Vietnamese SMEs, risk management, supply chain due diligence, LkSG, CSDDD.

Introduction

The globalization of supply chains has intensified the scrutiny of corporate responsibility, particularly regarding human rights and environmental standards. The German Supply Chain Due Diligence Act (LkSG) and the European Union's Corporate Sustainability Due Diligence Directive (CSDDD) represent legislative efforts aimed at enforcing responsible business conduct across entire supply chains. The Vietnamese SMEs, as integral components of these global networks, are confronted with challenges in aligning with these stringent requirements. This study investigates the readiness of the Vietnamese SMEs in implementing risk management practices in accordance with the LkSG and CSDDD, identifying gaps and concerning strategies for improvement.

Literature Review

Risk management in supply chains encompasses the identification, assessment, and mitigation of potential adverse impacts on human rights and the environment. The OECD Guidelines for Multinational Enterprises emphasize the critical role of due diligence in responsible business conduct [1]. The LkSG mandates companies to establish risk management systems, conduct regular risk analyses, and implement preventive measures [2]. Likewise, the CSDDD mandates companies to integrate due diligence into corporate policies and risk management systems [1].

The previous studies have shown that the SMEs often lack the resources and expertise to implement comprehensive risk management systems. Dao Xuan Hoi (2022) highlights the limited awareness and understanding of due diligence requirements among Vietnamese SMEs, attributing this to unpredictable disclosure of information and lack of targeted support [4]. The International Labor Organization (ILO) highlights the role of social dialogue in enhancing compliance with labor standards [5].

Methodology

This study employs a mixed-methods approach, combining quantitative surveys and qualitative interviews. A survey was conducted among 150 Vietnamese SMEs operating in sectors such as textiles, electronics, and agriculture to assess their awareness and implementation of risk management practices related to supply chain due diligence. Additionally, in-depth interviews were conducted with 20 SME managers and industry experts to gain qualitative insights into the challenges and opportunities faced by these enterprises.

¹ University of Labor and Social Affairs, Vietnam

² Bachelor of Law - Hanoi Law University, Vietnam. E-mail: nguyenthihongnhung4696@gmail.com (Corresponding Author)

Findings

Awareness and understanding of due diligence requirements

In the context of new regulations such as the German Supply Chain Due Diligence Act (LkSG) and the EU Sustainability Due Diligence Directive (CSDDD), Vietnamese SMEs' awareness and understanding of supply chain due diligence requirements remain limited.

Most Vietnamese SMEs are not fully aware of the legal obligations related to supply chain due diligence due to lack of information and specific guidance from the authorities [4]. As a result, the enterprises have yet to proactively develop and implement risk management systems in accordance with international standards.

In addition, an OECD survey (2022) showed that only about 35% of Vietnamese SMEs in Vietnam have a basic understanding of supply chain due diligence requirements. Of these, only 28% have begun implementing relevant risk management practices. The main reasons identified are lack of resources, expertise and support from the relevant organizations [6].

Implementation of risk management practices

The implementation of risk management practices in the small and medium-sized enterprises (SMEs), especially in the context of regulations such as the German Supply Chain Due Diligence Act (LkSG) and the EU Sustainability Due Diligence Directive (CSDDD), remains limited.

Limited resources and internal capacity

Most Vietnamese SMEs have not yet established risk management systems that meet the requirements of LkSG and CSDDD. The main reasons are lack of financial resources, specialized personnel and support from the relevant organizations. Many enterprises are not fully aware of the importance of integrating risk management into the overall business strategy.

Lack of specific policies and procedures

Only about 28% of Vietnamese SMEs in Vietnam have begun implementing risk management practices related to supply chain due diligence. Most enterprises have not yet developed specific policies and procedures to identify, assess and control risks in their supply chains. [1]This makes the enterprises vulnerable to fluctuations and new requirements from the international market.

Limited External Support

Despite some support programs from the international organizations such as the OECD, access and participation of the Vietnamese SMEs is limited. This may be due to lack of information, language barriers or lack of coordination among the stakeholders. The lack of external support makes it difficult for the Vietnamese SMEs to improve their capacity and implement effectively risk management practices.

Industry differences in the readiness of the Vietnamese SMEs to conduct supply chain due diligence

Implementing supply chain due diligence requirements under regulations such as the German Supply Chain Due Diligence Act (LkSG) and the EU Sustainability Due Diligence Directive (CSDDD) is creating different challenges for the Vietnamese SMEs, depending on the industry they operate in. This difference reflects the level of integration into global value chains, requirements from the international partners and access to resources of each industry.

Textile and footwear industry: Higher readiness level

The textile and footwear industry accounts for about 16% of Vietnam's total export turnover and employs about 2.5 million workers [6]. Due to the deep integration into the global supply chain and pressure from international brands, the Vietnamese SMEs in this industry have begun to apply supply chain due diligence practices [6]. The OECD has organized online workshops to guide the Vietnamese enterprises in this industry to apply OECD due diligence guidelines, helping them improve compliance and enhance sustainability in the supply chain [6].

Electronics and components industry: Slower implementation progress

Despite the high level of international integration of the electronics and components industry, many Vietnamese SMEs in this industry have yet to fully implement supply chain due diligence practices. This is mainly due to lack of information, resources and necessary technical support. Many enterprises in this industry are not fully aware of the due diligence requirements and have no specific plan to meet the international standards [4].

Agriculture and food processing sector: Low readiness

The Vietnamese SMEs in the agriculture and food processing sector are often small in scale, have fragmented operations, and lack the resources to implement risk management systems. Despite the sector's important role in the global food supply chain, many enterprises are not equipped with the knowledge and tools needed to conduct effectively supply chain due diligence. The OECD has implemented pilot projects to support the agricultural enterprises in Southeast Asia, including Vietnam, to improve their supply chain due diligence capacity.

Machinery and equipment industry: Lack of capacity and support

The machinery and equipment industry in Vietnam is facing challenges of high logistics costs and technical capacity shortages. Many Vietnamese SMEs in this industry are not able to implement supply chain due diligence practices due to limited resources and lack of support from the relevant organizations. The lack of training programs and technical support has prevented many enterprises in this industry from meeting the requirements of the international partners.

Role of external support for the Vietnamese SMEs in implementing supply chain due diligence

As the Vietnamese small and medium-sized enterprises (SMEs) face challenges in implementing supply chain due diligence requirements under international regulations such as the German Supply Chain Due Diligence Act (LkSG) and the EU Sustainability Due Diligence Directive (CSDDD), external support plays a key role in enhancing their capacity and compliance.

Support from the international organizations

The Organization for Economic Cooperation and Development (OECD) has implemented many programs to support the Vietnamese SMEs in Vietnam in conducting supply chain due diligence. Specifically, the OECD has organized online classes on Responsible Business and Risk-Based Due Diligence for the Vietnamese SMEs in Vietnam, providing knowledge about OECD guidelines and how to apply them in accordance with the characteristics of the Vietnamese SMEs. [7].

In addition, the OECD has also developed the Responsible Business E-learning Academy, which offers free online courses on supply chain due diligence in sectors such as agriculture, textiles and electronics, helping the Vietnamese SMEs access the knowledge and tools needed to conduct effective due diligence. [7].

Support from associations and NGOs

The business associations and NGOs also play an important role in supporting the Vietnamese SMEs. For example, the associations such as EuroCham, AusCham, BritCham and AmCham have collaborated with the OECD to organize workshops on building sustainable supply chains in the context of Vietnam, providing information and sharing practical experiences for the enterprises . [7] .

Support from government and state agencies

The Vietnamese government has also taken steps to support the Vietnamese SMEs in conducting supply chain due diligence. However, there are still barriers such as lack of financial resources, skilled personnel and timely policy support, affecting the ability of the Vietnamese SMEs to conduct due diligence. [9] .

Discussion

The small and medium-sized enterprises (SMEs) in Vietnam face specific barriers in their journey to comply with the German Supply Chain Law (LkSG). One of the biggest challenges is limited financial resources. Establishing effective risk management systems and complaints mechanisms requires significant investment, which many SMEs find difficult to afford compared to the larger enterprises. In addition, the SMEs often have more difficulty accessing the information and expertise needed to understand and implement the complex requirements of LkSG.

A further challenge for the SMEs is the limited availability of qualified and experienced personnel in the areas of risk management and compliance with international standards. The recruitment and training of qualified staff capable of implementing the LkSG requirements can be a burden for small enterprises. Furthermore, many SMEs may lack awareness of the strategic importance of LkSG compliance to their competitiveness and access to international markets. If SMEs cannot meet the standards set by the LkSG, they can be excluded from the global supply chain, leading to loss of business opportunities and affecting their sustainable development. This is particularly worrying as SMEs make up the majority of enterprises in Vietnam and contribute significantly to the national economy. Therefore, support programs need to be specifically designed to address the specific challenges faced by the SMEs face, helping them overcome these barriers and ensuring their effective participation in sustainable supply chains with Germany.

The findings indicate that the Vietnamese SMEs face significant challenges in aligning with the LkSG and CSDDD due to limited awareness, resource constraints, and lack of expertise. The Industry differences suggest that targeted interventions are necessary to address the specific needs of the SMEs in various industries. Moreover, the positive impact of external support underscores the need for collaborative efforts among the stakeholders to enhance the SMEs' capacities.

To improve readiness, the SMEs should be provided with accessible information, training programs, and practical tools tailored to their contexts. The Government agencies, industry associations, and international organizations play a pivotal role in developing and disseminating these resources. Additionally, integrating due diligence requirements into existing business processes can help the SMEs manage compliance more effectively.

An overall analysis of the risk management readiness of the Vietnamese small and medium-sized enterprises (SMEs) in the context of EU and German supply chain due diligence regulations reveals a mixed picture, reflecting both progress and challenges.

Awareness and understanding of supply chain due diligence requirements

As presented in section 4.1, the level of awareness and understanding of supply chain due diligence requirements is limited within the Vietnamese SMEs community. The main reasons are lack of information, specific guidance and support from the relevant organizations. Many Vietnamese SMEs are not fully aware of the importance of integrating risk management into their overall business strategy. This shortage could

result in the enterprises failing to meet requirements from the international partners, especially in the context of regulations such as LkSG and CSDDD being strongly implemented [4].

Implementing risk management practices

Section 4.2 has shown that the implementation of risk management practices in the Vietnamese SMEs in Vietnam is still limited. The main reasons are lack of financial resources, professional personnel and support from the relevant organizations. Many enterprises have not yet developed specific policies and procedures to identify, assess and control risks in their supply chains. This makes the enterprises vulnerable to fluctuations and new requirements from the international markets.

Industry differences

The analysis in section 4.3 shows clear differences across industries in their willingness to conduct supply chain due diligence. The textile and footwear industry, with its high level of integration into the global supply chain, has made certain strides in adopting due diligence practices. Meanwhile, industries such as electronics, agriculture and machinery and equipment still face many difficulties due to lack of resources and technical support. This suggests the need for industry-specific policies and support programs to enhance supply chain assessment capacity.

Role of external support

As presented in section 4.4, support from the international organizations, business associations and governments plays a key role in enhancing the supply chain assessment capacity of the Vietnamese SMEs. The OECD has implemented a number of programs to support the Vietnamese SMEs in conducting supply chain due diligence, including online classes and developing the Responsible Business E-learning Academy. However, there are still barriers such as lack of financial resources, skilled personnel and timely policy support, affecting the ability of the Vietnamese SMEs to conduct appraisals [9].

Recommendations

To improve the situation, it is recommended that there should be close coordination between the state agencies, industry associations and international organizations in providing information, training and technical support to the Vietnamese SMEs. The development of specialized training programs and the provision of practical support tools will help the enterprises improve their awareness and capacity to effectively conduct supply chain due diligence [4].

To raise awareness and facilitate compliance with the German Supply Chain Law (LkSG) for the Vietnamese enterprises, especially the small and medium-sized enterprises (SMEs), a series of comprehensive and synchronous measures need to be implemented.

First, it is necessary to develop and implement specialized and accessible training programs in Vietnamese that focus on the basic principles, requirements, and practical steps to comply with the LkSG. These programs should clarify the differences between the LkSG and other certification standards, and provide specific guidance on risk assessment, establishing grievance mechanisms and labour rights issues.

Second, comprehensive guidance documents, including handbooks, templates, and online materials, translated into Vietnamese, need to be developed and widely disseminated, providing step-by-step instructions and practical tools for implementing the LkSG.

Third, it is necessary to enhance cooperation and knowledge-sharing platforms between the Vietnamese enterprises and the German partners, facilitated by the organizations such as AHK Vietnam and VCCI, to promote mutual understanding and address specific compliance challenges.

Fourth, it is necessary to enhance the role of VCCI and the related industry associations in providing specialized support and legal advice. and sector-specific guidance to help the enterprises navigate the complexities of LkSG compliance.

Fifth, it is necessary to explore opportunities for financial and technical assistance programs, possibly through cooperation between the German and Vietnamese governments and the international development organizations, and financial institutions, to support the SMEs in implementing the necessary due diligence practices and complaint mechanisms.

Sixth, it is necessary to encourage the adoption of best practices in establishing and managing effective complaint mechanisms, based on international guidelines, and case studies, ensuring that they are accessible, transparent and culturally relevant to Vietnamese workers.

Finally, strategies need to be proposed to address the challenges associated with promoting independent unions and effective collective bargaining, taking into account the existing legal framework and international labour standards. This may include dialogue with the Vietnamese government and supporting initiatives that promote workers' representation rights and benefits within the existing legal context.

Industry differences in the readiness of the Vietnamese SMEs to conduct supply chain due diligence reflect the need for specific support policies and programs. For highly integrated sectors such as textile and footwear, further information and technical assistance should be provided to enhance due diligence capacity. For sectors with lower readiness such as agriculture and machinery, training and financial support programs should be implemented to help the enterprises develop and implement appropriate risk management systems. Collaboration between the government agencies, industry associations and international organisations is key to enhancing the supply chain due diligence capacity of the Vietnamese SMEs.

To enhance the role of external support, the close coordination between the international organizations, business associations and the government is important in providing information, training and technical assistance to the Vietnamese SMEs. Developing specialized training programs, providing practical support tools, and facilitating access to resources for the Vietnamese SMEs will help improve their capacity to conduct appraisals.

Conclusion

The Vietnamese SMEs are at a critical juncture in adapting to the evolving landscape of global supply chain regulations. While some progress has been made, significant gaps remain in awareness and implementation of risk management practices required by the LkSG and CSDDD. Addressing these gaps requires concerted efforts from multiple stakeholders to provide the SMEs with the necessary support and resources. By enhancing their risk management readiness, the Vietnamese SMEs can not only ensure compliance but also strengthen their competitiveness in the global market.

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