Impact of Coronavirus (COVID-19) - Feb 29 2020

Since mid-January 2020 when an outbreak of novel Coronavirus (Covid-19) first appeared in the city of Wuhan, in central China's Hubei province, the number of reported Covid-19 cases has risen to an estimated 82,000 globally, with more than 2,800 deaths. The number of infections in China appears to have moderated, and 32,000 people have recovered from the virus. In late February, however, the number of new cases outside China has risen significantly and quickly, particularly in South Korea, Iran, Italy and Japan. In total 68 countries and territories are currently affected. In Vietnam the initial cases were reported in late January, shortly after the outbreak in China. All 16 people initially reported as having contracted the virus have now recovered, and Vietnam appears to have been successful in containing the virus.

Vietnam took swift preventative steps to limit the spread of the virus, curtailing transport with those countries affected, putting people in quarantine and extending the school holidays. The authorities have also been active in informing the public on a daily basis about the virus, through social media and traditional media, and raising awareness of practical steps its citizens can take: such as washing hands and wearing masks if unwell.

Vietnam is an increasingly open economy and is a key part of Asia's manufacturing supply chain. Manufacturing accounts for about 16% of total GDP, and any disruption to the flow of intermediate and finished goods between Vietnam and China, Korea and Japan, representing 56% of the total imports of Vietnam, and 31% of its total exports, will impact GDP growth. That said, given Vietnam's manufacturing capability, relatively low labour cost, and transport connections, some companies are already looking at expanding their operations in Vietnam, as part of a 'China-plus-one' strategy. The other sectors most likely to be hit the hardest include tourism and aviation. In recent years Vietnam has emerged as a favourite destination for tourists, particularly from China and South Korea. In 2019 Vietnam received 18 million international arrivals, and in the first month of 2020 it welcomed 1.9 million, including 644,000 from China, 468,000 from Korea, and 79,000 from Japan. For as long as travel restrictions are in place, tourist arrivals will be impacted. As result, the Ministry of Planning and Investment (MPI) has forecast Vietnam's GDP growth to fall to a seven-year low of approximately 6% in 2020.

Since the Vietnam stock-markets re-opened after the Lunar New Year, at the end of January, there has been a broad based sell-off in equities, in line with that in many emerging markets. During February the MSCI EM index was down by 5.9%, and the Vietnam All Share index was down by 4.5%. The estimated decline in Net Asset Value for Vietnam Holding is approximately 3.5% in February. The Fund's top-ten holdings make up approximately 70% of Net Asset Value. The largest impact on our top-ten from Covid-19 is likely to be in Saigon Cargo Services (SCS, 5% NAV) as international cargo accounts for approximately 90% of SCS revenue, and this could see declines of 20-30% during periods of transport disruptions, and dislocated supply chains. Another portfolio company Vincom Retail (VRE, 3.7% NAV) is likely to experience a reduction in footfall through its shopping malls of 20-30%, which will put pressure on its tenants, though its direct revenue is largely protected through mid-term fixed contracts. We also expect to see some decline in store traffic impacting Mobile World (MWG, 8.3% NAV) and Phu Nhuan Jewelry (PNJ, 11.7% NAV), although the latter was reported as experiencing peak sales in January due to the Lunar New Year, and strong sales on a couple of special festive in February (including Valentine's Day). Impact on the other top-ten holdings is expected to be neutral at the current time, with real-estate companies Khang Dien House (KDH, 6% NAV) and Dat Xanh Real Estate (DXG, 4.3% NAV) not expected to see any fundamental declines due to Covid-19. Our largest position (FPT, 13.7% NAV) has a diversified revenue base from Education, Telecommunications and IT Services, each of which is well placed to deliver strong growth. In terms of the banking sector, net interest margins and credit growth is expected to be lower on the back of lower business activities in the first half of 2020. We expect that government owned banks and commercial banks will be encouraged to take measures to support businesses through lowering lending rates. Our core banking position MB Bank (MBB, 7% NAV) has just closed a private placement of approximately USD $75m in its stock, indicating support from institutional investors for this well managed bank. The Fund's portfolio is on an estimated forward P/E ratio of 9.6x and a Price-Earnings-Growth (PEG) ratio of approximately 0.5x. Furthermore, approximately 46% of the Fund's NAV is in stocks that are at their Foreign Ownership Limit (FOL). Many of these FOL stocks command a premium that ranges from 7% to 25% to the listed prices used in estimating the Net Asset Value.

Although it is not clear how widespread the virus's impact will be for Vietnam, or how long disruptions will persist, when normality eventually returns, there is likely to be a rapid rebound in domestic confidence, which would likely be reflected favourably in the domestic equity markets. After SARS, in 2003, China and other economies in Asia experienced a 'V' shape recovery, and this might be the same if and when Covid-19 is eventually brought under control. Vietnam ended 2019 on a high-note, with record levels of foreign currency reserves, and this can help buffer some of the short-term impacts.