PRESS CUTTINGS

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Emerging market economies offer Eastern promise

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China's slow growth has had a knock-on effect on most emerging markets in some way or other. However, there are some that seem to be soldiering on regardless.

One of these is India, where the low oil price is proving beneficial given the country's reliance on oil imports, and where exports to China were never really a big part of the economy.

Another is Vietnam. This may be more of a surprise – Vietnam is a producer and exporter of oil and other commodities. Its position on China's southern border, and its relatively cheap labour force, have made it a natural choice for low-cost manufacturing for many Chinese companies.

It ought to be suffering but, despite the headwinds, it seems to be doing okay – GDP growth is forecast to be 6.7% in 2016.

Common thread

In many ways, Vietnam and China have a lot in common. For example, both are ruled by communists that seem to have embraced capitalism, but in a way where the party has retained control of most of the levers in the economy.

However, Vietnam's economic transformation is some years behind China's – Vietnam's Socialist Oriented Market Model came about eight years after Deng Xioaping's reforms.

Its demographics are much more favourable to growth than China's: GDP per capita is a fraction of its larger neighbour and the state has been slow to relax its grip on many sectors of the economy.

Vietnam did manage to go through the debt splurge and consequent non-performing loan problem that currently afflicts the nation, but here it was some time ahead and the government is making slow but steady progress in addressing the situation.

On the upswing

A few years ago, the economy was plagued by bouts of inflation as inefficiencies caused price squeezes in some sectors and a large trade deficit weakened the currency. But this soon started to change. As manufacturing exports soared (post significant investment from the likes of Samsung, LG and Intel), the currency stabilised and inflation fell, aided by weak commodity prices. Government finances are now much more robust.

Foreign ownership limits for listed Vietnamese companies have also dampened flows in Vietnam's stock markets. Progress has been slow but the government is now allowing companies to set their own limits and change is happening.

The pace of privatisations is picking up too. As liquidity increases, the stock market ought to attract a wider range of foreign investors. This in turn should help narrow the valuation gap between Vietnam and its Asian neighbours.

Since PXP Vietnam unitised a couple of years ago, investors in closed-end funds wanting exposure to Vietnamese equities now have a choice between Vietnam Holding (VNH) and VinaCapital Vietnam Opportunities (VOF). Both trade on wide discounts – 16.7% for VNH and 22.8% for VOF.

VOF is by far the larger fund, with a market cap of more than £400 million against VNH's £78 million. VNH's smaller size helps inflate its ongoing charges ratio, which stands at 2.9% against 1.8% for VOF. VNH has outperformed VOF over most time periods, returning 28% over the past year (in NAV terms), while VOF has returned 23%. VOF is the one that I hold.

Virtue in Vietnam? Change is afoot in the economy

Down weighting

The main difference between the two funds is VOF's multi-asset portfolio. VOF was originally designed to have exposure to property and private equity, as well as listed equities. The property element has been a considerable drag on returns for many years now and VOF has been selling down exposure. A deal announced on 11 May (the sale of a stake in a large development site in Ho Chi Minh City) brings the property weighting down to 8%. Future performance should be much more geared to success within the private equity and listed portfolios.

The inclusion of private equity within the mix makes sense on a long-term perspective. There are some sectors that are harder to access through the listed market, and private equity ought to be much less susceptible to "hot money".

Inevitably, there will be times when the stock market is running up and the private equity portfolio acts as a temporary brake on performance, but VOF's analysis suggests the private equity portfolio exits have outperformed the listed portfolio over the medium term by quite a margin. If privatisations continue apace, VOF should benefit from a number of exits over the next few years and, hopefully, it will continue to do well. ●