

# Viet Nam Equity Special Access Fund (VESAF)

30 June 2017



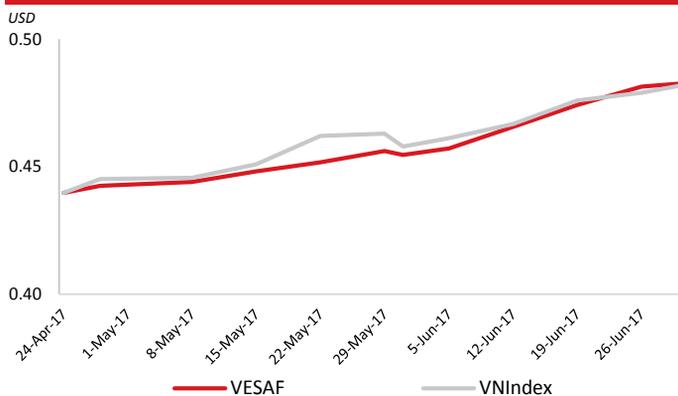
NAV/share: VND10,976 (USD0.482)

VESAF is a fund that invests in all equity opportunities unencumbered by foreign restriction or size. The strategy of the fund is to take meaningful stakes in companies with a robust franchise that we believe can benefit from the domestic growth of the country.

## PERFORMANCE SUMMARY

	Fund	VN Index
June 2017	6.14%	5.20%
Year-to-date	9.73%	9.55%
Cumulative since inception	9.73%	9.55%

## PERFORMANCE CHART



## TOP 5 HOLDINGS

TOP 5 HOLDINGS	SECTOR	NAV (%)	PE 2017 (x)	ROE (%)
FPT	Technology	14.0%	11.0	18.2
MBB	Banks	6.9%	10.9	12.0
VSC	Transportation	6.9%	10.3	16.3
MWG	Retailing	5.8%	15.4	37.1
BMP	Capital Goods	5.4%	13.5	23.5
<b>Total</b>		<b>39.0%</b>		

## EQUITY ALLOCATION

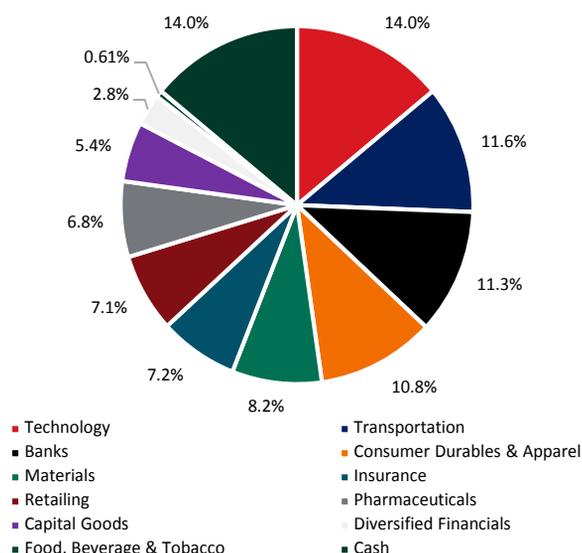
Small- & mid- cap stocks	58%
Stocks traded on UpCom	14%
Stocks at full Foreign Ownership Limit	73%

- Small- cap: stocks with market capitalization below US\$250 million
- Mid- cap: stocks with market capitalization from US\$250 million to US\$1 billion
- UpCom: Unlisted Public Company Market

## FUND INFORMATION

Structure	Open-ended fund
Launch date	25 April 2017
Fund size	VND83bn (USD3.7m)
Domicile	Vietnam
Valuation policy	NAV
NAV frequency	Weekly
Fund Manager	VinaWealth Fund Management JSC (a subsidiary of VinaCapital)
Auditor	Ernst & Young (Vietnam) Ltd
Administrator & Custodian bank	Standard Chartered Bank (Vietnam) Ltd
Management fee	1.75%
Subscription/Redemption frequency	Weekly on every Tuesday (T), requests must be submitted by 10:30am on T-1
Subscription charges	Subscription amount below VND2bn: 2% Subscription amount of VND2bn or above: 0%
Redemption charges	3% for the 1 <sup>st</sup> year; 1% for the 2 <sup>nd</sup> year; 0% after 3 years
Currency	VND

## SECTORS ALLOCATION



## MANAGER'S QUARTERLY COMMENTARY

VESAF had a successful first quarter with NAV/unit up 9.73% since inception on 25th April through 30th June 2017. This is an encouraging start as the fund recorded an outperformance despite launching in a fast rising market. As at the end of the quarter, the fund was 86% invested.

Our major focus to date has been to leverage the fund's ability to buy stocks that are unavailable to foreigners. These stocks generally have good fundamentals and strong growth potential, or are in strategic sectors. We also overweight small- and mid-cap stocks as they are often under the radar of ETFs and other large funds. Therefore they typically trade at compelling valuations while enjoying good growth prospects being leaders in their respective niche segments. We aim to run up to USD25 million in the next 12 months, enabling us to capture market inefficiencies. The market is still small and we recognize this by remaining small and nimble. A more detailed discussion of our key investment themes follows.

### ***Unconstrained by Foreign Ownership Limits***

The market is obsessed with privatization deals. Meanwhile, we are more measured and believe the real excitement lies in the opening of the market to foreigners rather than a mass privatization plan of state-owned enterprises from the government. VESAF is unique in that it is not constrained by the foreign ownership limit (FOL) regulation that applies to companies listed on Vietnam's stock markets. Therefore, the fund can invest in companies with no room for foreign investors. At present, 73% of our NAV is allocated to full-room stocks, such as FPT, VSC, MWG, PNJ and PVI. Most of these companies operate in industries that have sustainable growth and are favoured by foreign investors. Usually foreign investors have to pay a 7% - 30% premium to acquire shares in these companies, while VESAF does not.

Vietnam's stock market is on the road to liberalization. Since June 2015, foreign investors have been allowed to own up to a 100% stake in certain listed companies, depending on their business nature and shareholder approval to allow more foreign investors. Nevertheless, FOL removal has been slow, with only nine companies having removed their limits (and perhaps six more in 2017) since the government turned on the green light. This number is small when one looks at both the number of companies listed in Vietnam (709 on HOSE and HNX) and share of market capitalization (companies that have removed their FOL account for just 13% of total market cap). In most cases when the FOL is removed, we have seen a surge in share price both before and after such event.

Vietnam aims to be upgraded from a frontier market to an emerging market. Among the factors that is preventing it from being upgraded is the foreign ownership limit. There should be further legal reforms to clarify the process for removing FOLs, and we hope more companies will do so sooner than later. Nevertheless, we think that realistically the market will remain somewhat closed to foreign investors for the next three years. Therefore, VESAF has a great advantage over foreign funds in that it can access all of these crown jewel stocks without having to pay a premium. Since VESAF's inception, the full-room stocks in our portfolio have performed well (a return of 12% on average) and contributed 87% to our fund's performance. We believe that our strategy of holding full-room stocks will continue to be rewarded in the future.

### ***FOL Stock Case Study: FPT Corporation (FPT)***

FPT Corporation (FPT), which represents the highest weight in our portfolio, has gained 25% YTD and 20% since VESAF's inception. FPT, with a market cap of USD1.1 billion, is a leading technology company in Vietnam which operates in software, telecommunication, IT systems, and distribution of ICT products. Last year, the company achieved modest profit growth of only 3% y-o-y due to the expense of upgrading its broadband internet service to fibre-to-the-home (FTTH) and disruption in distribution of some mobile phone products, which were one-off events. We expect strong profit growth to return in 2017, which may reach over 15% y-o-y, and have overweighed FPT since the fund's inception. In fact, 5M17 business results of FPT were quite positive with pre-tax profit growing by 12% y-o-y, reaching USD51.4 million, in which the two major business segments, software outsourcing (30% of the group's profit) and telecommunication (45% of the group's profit), saw their profit advancing by 20% y-o-y and 21% y-o-y, respectively. The distribution business (10% of the group's profit) is still negatively impacted by last year's aforementioned event, but profit decline has been minimized since April 2017, so we should see higher profit growth in 2H17 for both the group and the distribution business.

A long-awaited catalyst for FPT will materialize this year: the company will sell its distribution (FPT Trading) and retail business (FPT Retail), either partially or fully. Initial investments of FPT in FPT Trading and FPT Retail were USD30 million (100% stake) and USD7.5 million (85% stake), respectively, and the two subsidiaries generated net profit of USD10 million and USD9.1 million in 2016. It is anticipated that the two businesses combined can be valued at over USD200 million, enabling FPT to record significant profit from the divestment. More importantly, the proceeds can be re-invested in the software and telecommunication businesses. At present, FPT is trading at only 11x FY2017f P/E. Exiting from the distribution and retail businesses will turn FPT into a pure technology company, deserving a higher valuation.

Over the long term, software and telecommunication will be the two pillars of FPT. During 2012-2016, the two businesses achieved profit CAGR of 22% and 8%, respectively. FPT is now going global with clients in 21 countries. In 2016, 31% of its profit was generated from overseas market with annual growth rate of 40%. The company is embracing new technology trends, such as SMAC (social, mobile, analytics and cloud) and IoT (internet of things) and its software business aims to grow by 30% annually in the next three years. In the domestic market, increases in ICT spending by both the government and private sectors, and below-average penetration rate of broadband internet will create business opportunities for FPT.

### **Small Cap Case Study: Hoa An Joint Stock Company (DHA)**

Our portfolio overweights small- and mid-cap stocks which are characterized by high growth (being beneficiaries of Vietnam's industrialization and growing consumption), high ROE, compelling valuations, and being under-researched. At present, small-cap stocks account for 29% of our portfolio. They are trading at trailing P/E of 10.4x (vs. VN Index of 16.6x), and are expected to attain 21% profit growth in 2017. Despite being small in terms of market cap, all of them are leaders in certain industries or have unique competitive advantages. We are looking for new investment opportunities and aim to add another five to six small-cap stocks into VESAF.

One of our early choices is Hoa An JSC (DHA), a stone mining company with a simple business model but good profitability. DHA supplies stone to construction projects, including residential, industrial and infrastructure. It owns three stone mines in Dong Nai province, at the center of the "industrial triangle" in southern Vietnam (Ho Chi Minh City, Dong Nai and Binh Duong). According to GDP data from the General Statistics Office, the construction industry grew 10.8% in 2015, 10% in 2016 and 8.5% in 1H17, and the "industrial triangle" typically achieved the highest growth nationally.

In fact, during 2013-2016, revenue and net profit CAGR of listed stone mining companies in the area reached 14% and 32%, respectively. Looking ahead, we see sales growth supported by numerous infrastructure projects, such as the highway and road network, the metro lines, upgrade of Tan Son Nhat International Airport and the massive development of Long Thanh International Airport. In addition, residential construction is expected to maintain stable growth thanks to increasing income per capita, population and urbanization in the region.

Among listed stone mining companies, we chose DHA because of the tenure of its mining licenses. Its mines are permitted to be exploited over the next ten years, while mine licenses of other companies will expire in the next two years, and renewal is uncertain. In addition, DHA may have the highest earnings upside in 2017. Firstly, sales volume will increase from a low-base in 2016, when the collapse of a bridge on the Dong Nai River obstructed the company's waterway transportation system. Secondly, the company's new mine, Tan Cang 3, which accounts for approximately 30% sales of the company, will be much more profitable in 2017. Last year, profit of Tan Cang 3 was minimal because the company had to bear the expense of removing the covering soil layer and upper stone has lower quality, hence lower selling price. DHA is expected to achieve 30% net profit growth in 2017 and now trading at 8.1x FY2017f P/E. The stock gained 12.2% in June 2017 and 11.9% since VESAF's inception.

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#### **Disclaimer**

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