



## AFC VIETNAM FUND UPDATE

<b>Fund Category</b>	Vietnam Public Equities
<b>Country Focus</b>	Vietnam
<b>Subscriptions</b>	Monthly at NAV (five business days before month end)
<b>Redemptions</b>	Monthly at NAV 60 days notice
<b>Benchmark</b>	VN Index
<b>Fund Manager</b>	Andreas Karall
<b>Investment Manager</b>	Asia Frontier Capital (Vietnam) Ltd., Cayman Islands
<b>Investment Advisor</b>	Asia Frontier Investments Ltd., Hong Kong
<b>Fund Base Currency</b>	USD
<b>Minimum Investment</b>	USD 10,000
<b>Subsequent Investments</b>	USD 1,000
<b>Management Fee</b>	1.8% p.a. of NAV
<b>Performance Fee</b>	12.5% p.a. of AV appreciation with high watermark
<b>Fund Domicile</b>	Cayman Islands
<b>Launch Date</b>	23 December 2013
<b>Custodian Bank</b>	Viet Capital Securities, Ho Chi Minh City
<b>Auditor</b>	EY, Hong Kong
<b>Administrator</b>	Custom House, Singapore
<b>Legal Advisor</b>	Ogier, Hong Kong
<b>ISIN</b>	KYG0133A1673

### Contact Information

**Asia Frontier Capital Ltd.**  
www.asiafrontiercapital.com

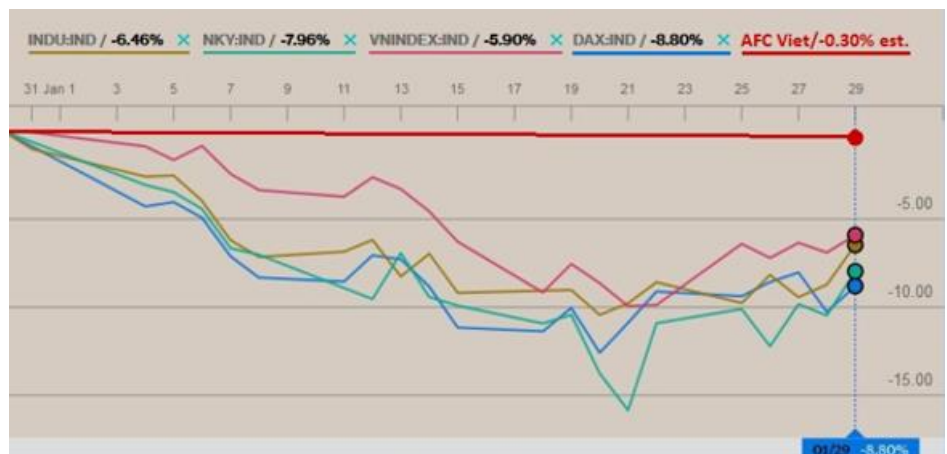
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January is historically a strong month and I don't dare to imagine what would have happened if this year's January scenario would have happened in the historically weak September month... For many exchanges this was the weakest January since 2009, and the major stock markets ended the month with a loss of 6-9% (Shanghai even -23%) but some of them were down more than 10% at some point during the month (e.g. Tokyo -16%). Also Vietnam went through a significant correction at around the middle of the month but the two indices recovered slightly and closed the month at -5.8% in Ho Chi Minh City and -3.9% in Hanoi. There was already a fair amount of our companies which reported their 2015 results and many of them were better than our expectations. With some of those stocks rising against the trend our total losses were very limited. Emerging market currencies were generally weaker against the USD but the Vietnamese Dong was bucking this trend and strengthened about 1% versus the USD. According to internal calculations the current NAV lost only 0.3% in January and stands now at approximately USD 1,414.



Source: Bloomberg

The reasons for this bumpy start of the year are not really easy to understand. The fact that many banks will probably be hit with bad loans from the energy sector shouldn't come as a big surprise. The constant fear of a "hard landing" in China is neither new nor sustainably proven. The massive capital outflows from China, which are often called as one of the main reasons for the current skepticism about China, can be refuted according to the latest figures from BIS (Bank for International Settlements). Both the short- as well as long-term USD liabilities of Chinese companies fell by 60% and 20% respectively and are the main reason for this outflow. This would be very positive in the medium term and absolutely risk averse! Also debates that economic statistics in China are to be treated with caution and that they are sometimes manipulated is highly likely – but that was the same for the past 20+ years. But on the other hand - are western economic data like for example inflation numbers always really trustworthy? Undoubtedly, the Chinese economy is slowly but surely, by orders from the "top", transforming from a cheap manufacturing and export oriented model to a western style consumer driven society. Meanwhile, 40% of the economic output will be already borne by domestic consumer. Consumption is booming in contrast to industrial production and it is estimated to grow by 8-10% in the coming years. In other words - even with a stagnation of the industry, the basic growth is already at 4% and the demand for all types of raw materials from Chinese consumer (as of course as well from other "new" consumers of emerging economies) is constantly increasing.

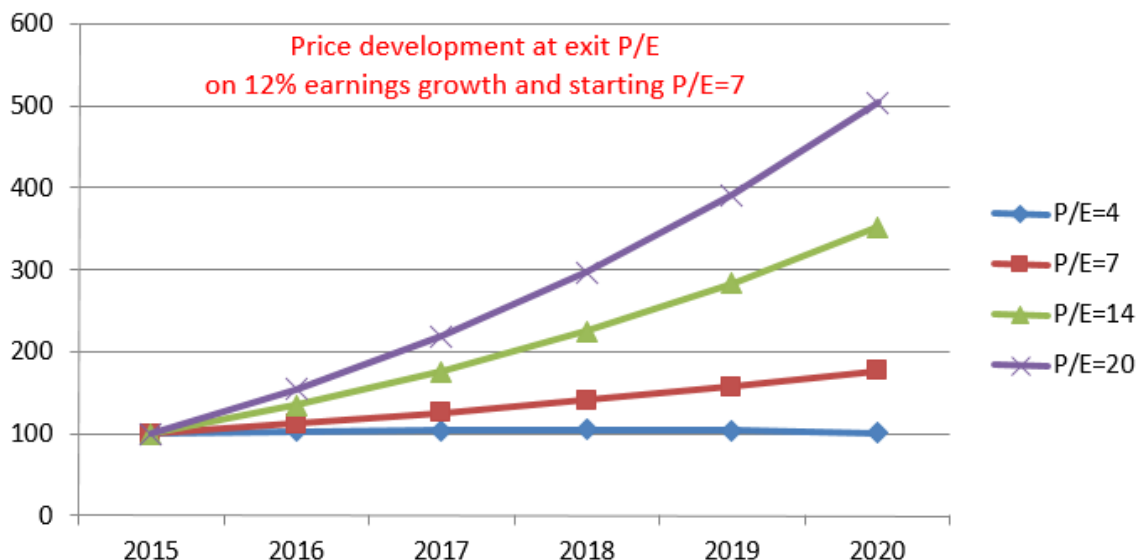


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Vietnam however is still about 15-20 years behind China's development and benefits from the shift of production from China to Vietnam. Due to the difference in size between those two countries, already a few percentage points of this "manufacturing shift" are sufficient to keep the growth in Vietnam at a very high level, even with a weaker growth internationally, as long as the domestic demand can be maintained at a reasonable level. It is impressive to note that the economic recovery in the major cities such as Ho Chi Minh City with about 10% is significantly higher than in the rest of the country, where a growth rate of 6.5 - 7% for the next years can be expected.

One could easily draw the conclusion that with falling raw material prices of up to 75% over the past 18 months the demand has fallen accordingly. This however is far from the truth with a world economic growth of around 3%. Global oil consumption has actually increased by about 12% over the past 10 years. It is therefore also misleading to look at the falling oil prices as a sign of an ailing world economy. The current oil price decline is not attributable to a collapse in demand, but rather to politically motivated production increases. Economic hardship of some oil producing countries also doesn't allow them to reduce production. We are therefore witnessing the greatest wealth redistribution in recent decades - away from some oil-producing countries (2/3 of the world's oil production has its origin from 10 countries) towards other countries and companies and of course a large portion of the world's population which are benefitting from falling energy prices.

Due to the recent turmoil in global markets, the average valuation in Vietnam is now even more attractive than at the launch of our fund, but we are also conscious of the fact that this situation might not last for very long and that the bull market in Vietnam will return sooner rather than later. The overall market with a PE of 11x is valued very favourable in comparison to international markets, but our portfolio has now a valuation of only around 7 times earnings. Vietnam certainly has a lot of upside potential over the coming years, given the sound fundamentals supporting strong economic growth, but the revaluation process of our holdings from currently undervalued levels will attribute significant value to our fund. This revaluation process has already started 3 years ago in the small- and mid-cap segment and we expect that this will continue. With a realistic 12% annual profit increase (hopefully even higher!) the below chart clearly shows that the biggest impact of the value creation is the revaluation effect. A PE of 14x would be below average in Asia, 20x would be a typical bull market with an optimistic outlook, as expected for the coming years. Whether Wall Street or Europe, after years of nicely performing stock markets, are declining by 20 or 30% (most markets already lost 15-20% from their peak last year), should not really bother us in the long term.

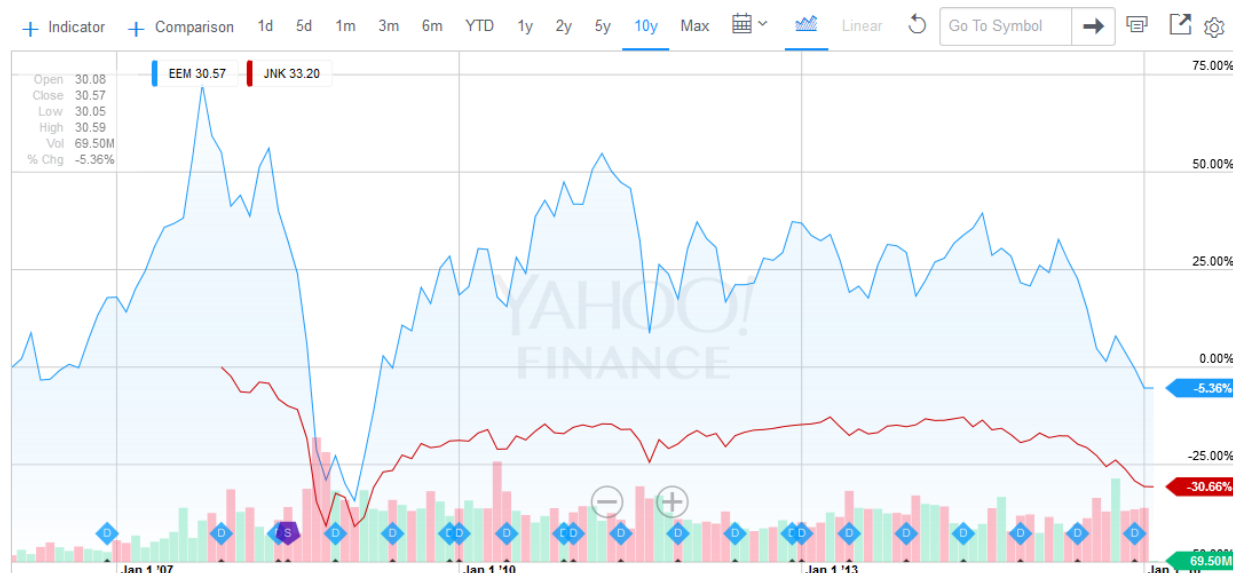


Source: AFC

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The Communist Party in Vietnam elects every five years their new leadership. The current reformist and Prime Minister Nguyen Tan Dung has come up to the maximum reign of 10 years and he therefore flirted with the job as the Party Secretary General. Unfortunately, this has not worked out, because on one hand he has already exceeded the maximum age limit of 65 years for the job and on the other hand he got not enough support from the party to grant him an exception to this rule. The current Party Secretary General Nguyen Phu Trong was re-elected and the former Deputy Prime Minister Nguyen Xuan Phuc will most likely be the new Prime Minister. It is generally expected that economic reforms will continue and that there will be no major changes in direction in the policy of Vietnam.

While many investors are afraid of a repetition of the global financial crisis (GFC) of 2008/2009 and refer to the credit and emerging markets, we find it amazing that these discussions are taking place at a time when both markets are already trading close to the lows of GFC and are far from exaggerated valuations as seen in 2007/2008.



Source: Yahoo, Inc.

The numerous frontier and emerging countries are ever so often all put in one basket without differentiation even though they are from different regions, governments and economic developments - even more pronounced than in the developed economies. A 5-year comparison therefore shows the enormous variations in performance from Russia to Brazil to the Philippines, ranging from -60% to +70%. The performance of China would have been completely unspectacular, if the short term hype of 2014/15 would not have taken place; but which now has been corrected. The beginning of Vietnam's outperformance in 2013, despite an overall weak absolute return, can clearly explained with the favourable valuations, the high economic growth and recovery in corporate earnings.

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Source: Bloomberg; Countries from top to bottom: Philippines, USA, Vietnam, China, Chile, Brazil, Russia

Vietnam's stock market is the most inexpensive in the region, its economic growth is the highest in the region and our job is therefore simply to continue to search for companies with favourable valuations and good perspectives. It is therefore a top priority for us to analyse yearly company results which are published these days. To date around one third of all listed companies and about half of all our holdings have announced their results. The results of our companies were slightly above our expectations and we see that the market rewards this positively and therefore continues to support our outperformance. In difficult situations, investors often sell investments at a profit to compensate for losses in other investments. Therefore, we are particularly pleased with the response of many new investors interested in the investment story Vietnam and our funds - we share their enthusiasm!

The subscription deadline for this month will be on the 23rd of February and if you would like any assistance with the investment process please be in touch with myself or Andreas Vogelsanger.

Best regards,

Andreas Karall, CIO

*\*The representative of the Fund in Switzerland is Hugo Fund Services SA, 6 Cours de Rive, 1204 Geneva. The distribution of Shares in Switzerland must exclusively be made to qualified investors. The place of performance and jurisdiction for Shares in the Fund distributed in Switzerland are at the registered office of the Representative.*

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