

AFC VIETNAM FUND UPDATE

Fund Category	Vietnam Public Equities
Country Focus	Vietnam
Subscriptions	Monthly at NAV (five business days before month end)
Redemptions	Monthly at NAV 30 days notice
Benchmark	VN Index
Fund Manager	Vicente Nguyen
Investment Manager	Asia Frontier Capital (Vietnam) Limited, Cayman Islands
Investment Advisor	Asia Frontier Investments Limited, Hong Kong
Fund Base Currency	USD
Minimum Investment	USD 10,000
Subsequent Investments	USD 1,000
Management Fee	1.8% p.a. of NAV
Performance Fee	12.5% p.a. of NAV appreciation with high watermark
Fund Domicile	Cayman Islands
Launch Date	23 December 2013
Custodian Bank	Viet Capital Securities, Ho Chi Minh City
Auditor	Ernst & Young, Hong Kong
Administrator	Trident Fund Services, Hong Kong
Legal Advisor	Ogier, Hong Kong
ISIN	KYG0133A1673

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The winning streak for the index continued in May, bringing strong gains for another month, with foreigners once again on the wrong (selling) side. Trading volume continued to be in record territory, but market breadth was weak as interest was concentrated in financial stocks. Banking stocks also helped our fund portfolio which performed +6.2% to an NAV of USD 2,802 according to internal estimates, versus an index gain of +7.2%. The latest wave of COVID-19 infections still seems to be well contained with daily numbers reaching 100-300 cases. Fast acting government measures, such as the recently announced social distancing implementing measures in HCMC, do not lead us to see changes to the economic forecasts for this year.

Market Developments

Despite renewed foreign selling throughout the month, the index continued its way to new highs, beating most other markets around the world. One of the likely reasons for the continued negligence could be the general assumption that Emerging Markets could see a weaker or slower recovery in economic activity as many Asian countries are pretty much closed for travel and are behind in vaccination rates compared to the Western world. Certainly, the new COVID-19 wave in many Asian countries did not help, but even the highest numbers in Vietnam with 100-300 daily new infections have to be seen in relation to the almost 100 mln population. On a positive note, the recent surge in cases was also a wakeup-call for politicians in these countries and efforts to secure vaccine supplies and start vaccinating the broader population has increased significantly in recent weeks.

As Vietnam is just a tiny financial market within the Asian Emerging Market and Frontier universe, people simply do not differentiate much and throw out the baby with the bathwater. By any economic comparison, measured both from the crisis year 2020, as well as the outlook for 2021 and beyond, Vietnam is ranked in the top countries in the world.

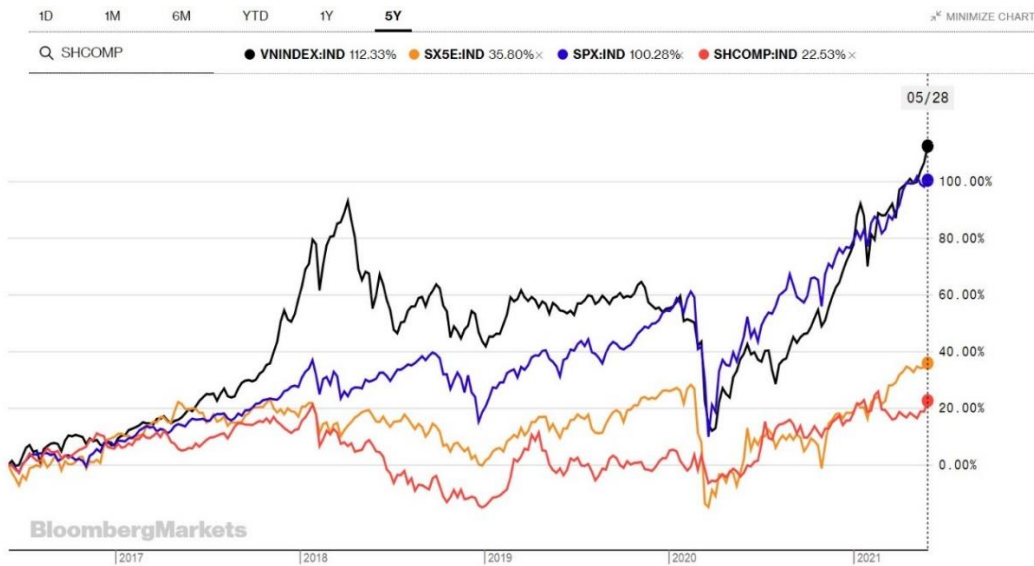
This is also – thankfully for our investors - reflected in the performance of the stock index, short- and long-term. While China (the Shanghai Composite) lagged significantly this year, Europe (the EURO STOXX 50) performed better than the US (S&P 500), but all three indexes are clearly trailing Vietnam (HSX) so far in 2021.



(Source: Bloomberg)

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More importantly, our bullish long-term stance on Vietnam is also bearing fruits as can be seen on the five-year performance where interestingly Vietnam has beaten the US market, while China and Europe showed a surprisingly high correlation.



(Source: Bloomberg, VietCapital Securities)

Despite fragmented smaller lockdowns over the past year, the positive attitude from Vietnamese is still unbroken, as can be seen from the consumer confidence index which ranks consistently much higher than global average. Together with the strong demand for products made in Vietnam, this is the backbone of the continued strong economic development.

Inflation – a threat for the world?

In recent weeks, business media has increasingly reported about the rising risk of the return of inflation, and some fear that central banks around the world would ignore it for too long altogether. While the ghost of inflation has been painted on the wall too many times over the past 20 years, the current period can hardly be compared to any other in the past 40 years.

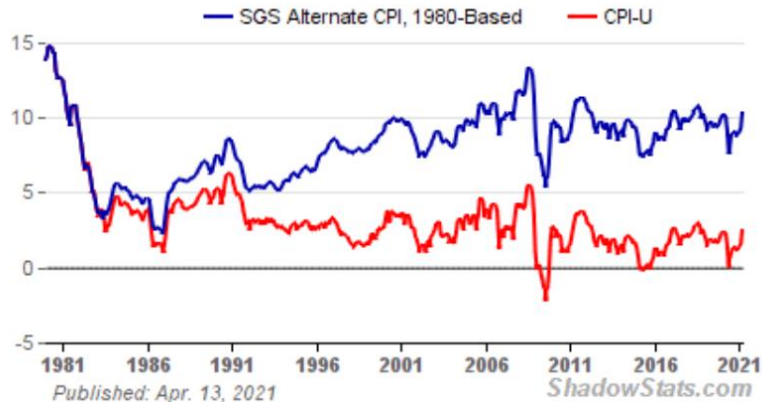
Most central bankers still speak of “temporary inflation” which will subside in the near future without the need to raise interest rates soon or by much, but this reminds us a bit of Trump’s statement last year that “the virus will disappear magically”. The fact is, that for 40 years, when the inflation phase of the 70’s was overcome, inflation had only a brief moment in 2008, while interest rates have known only one way over the years – down.

As with all statistics, these are only as good as their database is - and as long as it is comparable. The inflation calculation method has been changed a few times since 1980, to adjust for technological advances and changing spending habits. It is certainly true that prices for computers, TV’s, communication prices, etc. have fallen, but nobody would buy a five-year-old computer or TV, not to speak of an iPhone 7. The absolute amount of money we are spending now on computers or TVs has likely gone up somewhat compared to 20 years ago. The composition of the basket for consumer costs, including housing, is also questioned by many, especially by the consumers themselves. It is not much of a surprise that many people like to know the inflation rate, if not adjusted time and time again. Many middle-income earners would likely agree more on that rate than the official consumer inflation statistic.

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Consumer Inflation - Official vs ShadowStats (1980-Based) Alternate

Year to Year Change. Through Mar. 2021

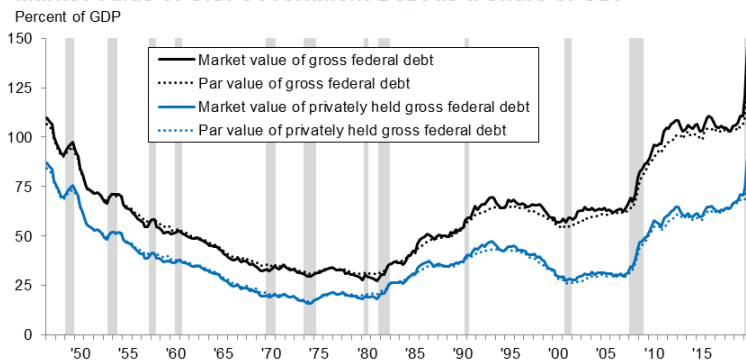


(Source: ShadowStats, CLSA)

Prices, and at least as important, interest payments for consumers, companies and governments were held in check by two crucial components – ever lower global interest rates and outsourcing of production to low-income countries mainly in Asia. But with all those long-term trends stretched (record low or negative interest rates, rising salaries in low-cost producing countries, logistical efficiency improvements like just-in-time production, etc.), where should we go from here? The COVID-19 crisis just accelerated the possible turnaround of those decade-long trends. Spending cuts and fights over budget allocation to sectors like health care or education were top priorities of governments, whereas 2020/21 will be seen as a historical moment in financial history where financial supports and helicopter money easily outstripped the financial crisis of 2008/09.

Since money is still “cheap”, global debt levels have increased sharply, with governments, companies and consumers paying hardly any interest on their debts. But this will also limit the future ability for central banks to normalize interest rates again as it should be done in a regular economic cycle when the economy recovers strongly and inflation is on the rise.

Chart 1B
Market Value of U.S. Government Debt as a Share of GDP



NOTE: Gray bars represent recessions.

SOURCES: U.S. Treasury; Federal Reserve Bank of New York; Wall Street Journal; Bloomberg L.P.; Bureau of Economic Analysis; Federal Reserve Bank of Dallas calculations.

As can be seen below from the 10-year US-treasury bond chart from 1962 until today, the debt level today is 3x higher than in the early 60's when interest rates were much higher than today and therefore servicing that debt was much harder. Not many governments would be able to survive interest rates we have seen in the past, not to speak of many companies and consumers which are also only able to spend because of this low interest rate environment.

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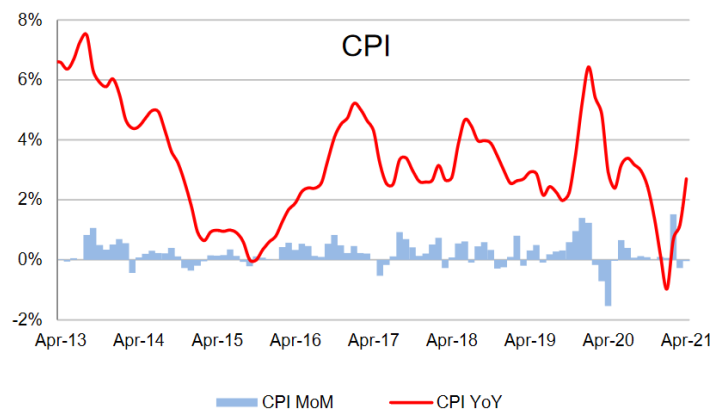
(Source: Yahoo Finance)

Since we do not expect central banks to commit financial suicide and also push a good percentage of their population over the “financial cliff” into bankruptcy, the most likely outcome is a continuation of negative real interest rates – and hoping that many of the current inflationary signs are really only temporary and will subside as worldwide production and shipments normalize.

Nevertheless, we should see a discontinuation of the global trend of production outsourcing as the world currently recognizes the risks of too much dependency that a few global players are producing most of the necessary products in certain parts of the world. The recent surge in prices for many commodities and shortages in certain sectors such as electronics is also a reason to have a close look at this development.

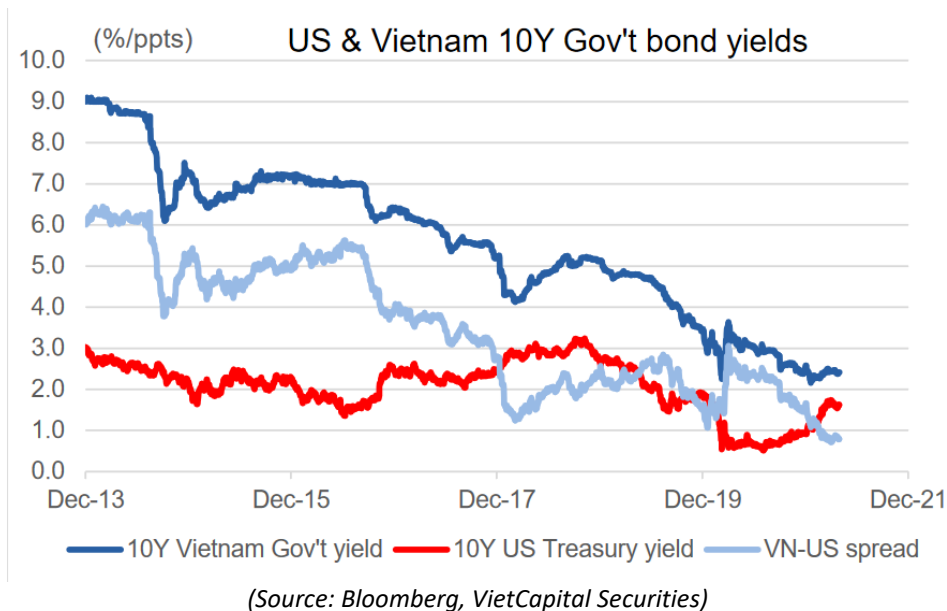
Vietnam and inflation

Unlike most parts of the world, emerging economies like Vietnam have more recent experience with inflation. During the bubble in 2008, inflation peaked at 28%. Only in recent years have Vietnam and other emerging markets shown quite acceptable levels of inflation. The recent rise can so far be seen as a normalization to the 5-year average after the brief negative value last year, and anything up to around 4% is not a cause for concern.



(Source: Bloomberg, VietCapital Securities)

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Historically, higher interest rates were accompanied by falling prices for most stocks and bonds, and surging interest in investments seen as a vault of wealth. As a store of value, usually gold comes to mind, followed by real estate which should keep its value, but with potentially stretched consumers not being able to pay back their mortgages, real estate prices eventually could also come under pressure. It is hard to tell if cryptocurrencies would offer any protection which in theory they should, but given their short history of existence, it is simply too speculative to be certain of that. Equities on the other hand, and this is most important for us, should see a mixed picture. Loss making startups in constant need of capital will be hit hardest, while cash rich, healthy companies offer good protection, and certain sectors will even benefit from rising pricing power.

We therefore are analyzing our portfolio very thoroughly in order to make potential adjustments, although we certainly do not want to make a bet on inflation. In our investment process we already look out for financially sound companies, so we simply want to reduce sector risks and find new ones or increase current positions where we see positive developments in the current environment.

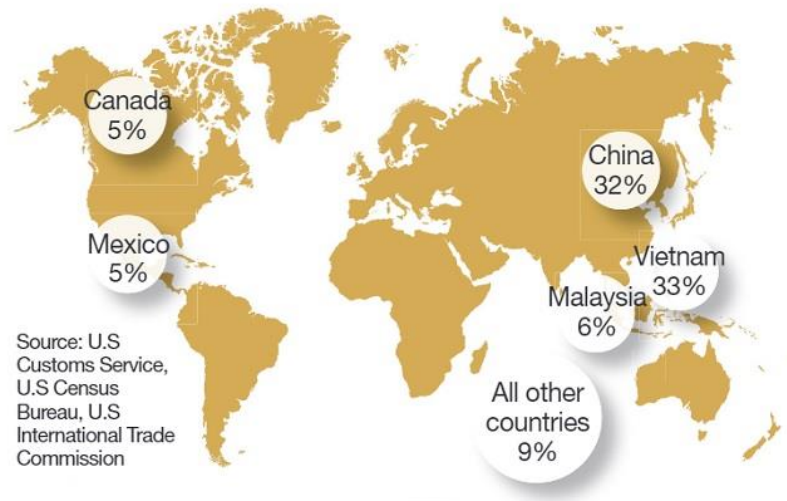
One of these examples is Phu Tai (PTB), which is one of the largest furniture exporters in Vietnam. The fact that demand for furniture in the US surged during COVID-19 and the trade war between China and US, helped Vietnam's furniture exports.

Vietnam surpassed China to become the largest furniture exporter to the US

We have recently witnessed a dramatic shift of furniture imports in the US, where Vietnam has overtaken China as the largest exporter of finished goods to the US market. According to "Furniture Today", Vietnam shipped slightly over USD 7.4 bln of furniture to the US in 2020, up 31% from USD 5.7 bln in 2019. By comparison, China shipped USD 7.3 bln in 2020, down 25% from the USD 9.7 bln in 2019.

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► Breakout of U.S furniture imports, 2020 By source country



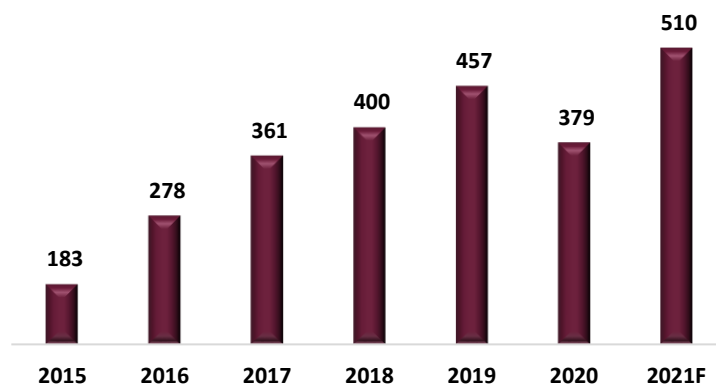
“That doesn’t surprise me at all,” said Fred Henjes, CEO of Riverside Furniture Corp. “We are no longer buying product out of China, and I know there are many others besides us.”

The main reasons for China’s decline in furniture exports to the US is driven by the antidumping duties and the (China) tariffs. Vietnam is creating production capacity, but they still have a long way to go, especially for upholstery products.

Phu Tai, as one of the largest furniture exporters in Vietnam, has benefited from this trend. The company has a very strong management team, and when they realized the upsurge in furniture demand from the US in 2017 and 2018, they decided to acquire several furniture factories in Vietnam in order to expand their capacity aggressively. In the first quarter of 2021, PTB revenues from furniture exports jumped 36% and total net profits gained 65%. The furniture business continued to grow continuously over the last 4 years, since the US tariffs on Chinese products were applied. In 2017, furniture contributed only 33% of total net profits and the stone business stood at 57%. But in the first quarter of 2021 the furniture business surpassed their stone business and contributed 68% of net profits.

We think Phu Tai is still undervalued with a trailing PER of 10x and forward PER of around 7.9x with an estimated earnings growth for the next five years of around 20% per annum.

Net profit of PTB in the last 5 years (VND bln)



(Source: PTB, AFC research)

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Key financial ratios of PTB

Key ratios		Last 12 months
Net revenue	VND bln	5,794
Gross profit	VND bln	1,237
Net profit	VND bln	398
ROE	%	19.5
PER	X	10.2
P/B	X	2.0
Div yield	%	3.4
EPS growth (last 5 years)	%	15.6

(Source: PTB reports, AFC research)



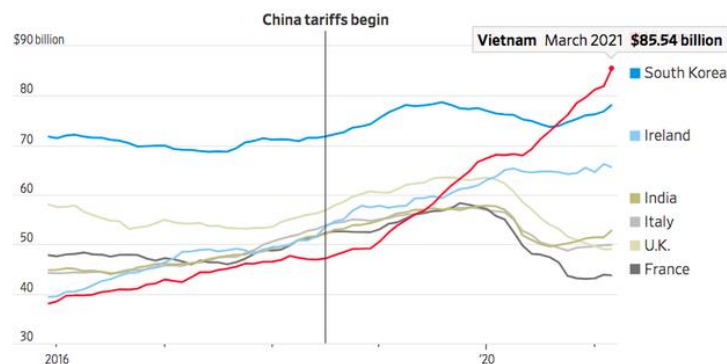
(PTB from March 2020 to May 2021; Source: VietCapital Securities)

Of course, Vietnam's exports to the US in general are benefiting from the trade war between China and US. According to the Wall Street Journal, Vietnam has risen to the 6th position in terms of US imports, a marked improvement from 12th position in 2018. Vietnam surpassed South Korea, Ireland and India with nearly USD 86 bln of exports to the US in the last 12 months.

Vietnam Rising

Vietnam has leapfrogged several major trading partners in Europe and Asia in recent years, and is now the sixth largest source of U.S. imports.

Exports to the U.S., 12-month rolling sum



(Source: Wall Street Journal)

The US tariffs on Chinese goods will most likely not disappear overnight even with the new president, Joe Biden. President Biden sees China as a serious competitor to the US economy and we therefore still see strong foreign direct investments into Vietnam in order to avoid punitive US tariffs. Besides key export products to the US, other sectors are benefiting from this trend such as port and logistics, industrial parks, construction and other accessories manufacturing sector.

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Summer holiday

With summer approaching, people around the world are eager to escape from the depressing months where most countries experienced various lockdowns and travel restrictions. Europe and the US are in a better position this year as most countries are expected to have the majority of their population vaccinated by this summer, enabling them to travel again to many parts of the world, although still with limitations and restrictions. Tourism was weak last year, with any (partly) normalization in the Western world expected to have a positive effect on their economies, while still sharply down from 2019. Vietnam – along with many other Asian nations – are still mostly closed for tourism and will experience another dull summer season. What many people forget when they think of the economic consequences is that beside another year of low tourism numbers and difficulties for the sector, the total impact on GDP growth will be marginal since weak 2021 numbers will be compared to next to zero 2020. A significant rebound in those countries is then expected for next year with all the positive impact on 2022 GDP.

Let us hope that after an improved summer holiday season this year, we will see the organized comeback on European beaches, as well as the less organized comeback on Vietnamese beaches again in 2022!



(Rimini; Source: Wikipedia)

(Vung Tau; Source: vnExpress)

Economy

Macroeconomic Indicators				
	2018	2019	2020	May-21
GDP	7.08%	7.02%	7.30%	4.48%
Industrial production (YoY)	10.2%	8.9%	3.4%	9.9%
FDI disbursement (USD bln)	19.1	20.4	20.0	7.2
Exports (USD bln)	244.7	264.2	281.5	130.9
Imports (USD bln)	237.5	253.1	262.4	131.3
Trade balance (USD bln)	7.2	11.1	19.1	-0.4
Retail sales (YoY)	11.70%	11.80%	2.60%	7.60%
CPI (YoY)	3.54%	2.79%	3.23%	1.29%
VND	23,175	23,230	23,108	23,048
Credit growth (YoY)	13.9%	12.1%	10.5%	3.3%
Foreign reserves (USD bln)	60	73	92	94.8

(Source: GSO, VCB, State Bank, AFC Research)

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Subscription

The next subscription deadline will be 24th June 2021. If you would like any assistance with the subscription process please be in touch with Andreas Vogelsanger.

Best regards,

AFC Vietnam Fund

Estimated NAV as of 31st May 2021

NAV	2,802*
Since Inception	+180%*
Inception Date	23/12/2013

Monthly Performances AFC Vietnam Fund

		Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
2013	USD												+2.37%	+2.37%
2014	USD	+8.75%	+4.50%	+2.18%	-4.65%	-0.32%	+1.45%	+1.86%	+5.49%	+3.87%	+2.83%	+2.50%	+0.60%	+32.50%
2015	USD	+0.44%	+1.76%	-0.96%	+1.93%	-0.48%	+0.06%	+0.22%	-4.57%	+1.18%	+6.90%	-1.82%	+0.25%	+4.62%
2016	USD	-0.10%	+3.30%	+1.28%	+3.17%	+1.40%	+4.97%	+3.0%	+0.13%	+0.11%	-1.83%	+0.88%	-1.76%	+15.29%
2017	USD	+1.90%	+1.10%	+1.94%	+1.03%	+2.96%	+4.52%	+1.94%	-4.38%	+1.09%	-0.75%	+1.47%	+0.01%	+13.33%
2018	USD	+0.41%	+0.42%	+0.58%	-0.93%	-3.24%	-0.12%	-1.28%	+0.79%	+3.02	-2.14%	+0.45%	-2.05%	-4.17%
2019	USD	-1.63%	+2.90%	+1.58%	+0.82%	-3.35%	+1.98%	+1.18%	+1.63%	-1.89%	-2.34%	-1.59%	+2.31%	+0.70%
2020	USD	-1.41%	-3.93%	-18.44%	+12.72%	+4.28%	-0.28%	+0.78%	+8.65%	+6.02%	+0.72%	+6.91%	+12.77%	+27.66%
2021	USD	-1.89%	+9.49%	+5.84%	+1.58%	+6.2%*								+22.6%*

*According to internal calculations

**The Fund has appointed ACOLIN Fund Services AG, succursale Genève, 6 Cours de Rive, 1204 Geneva, Switzerland, as its Swiss Representative. NPB Neue Privat Bank AG, Limmatquai 1, 8024 Zürich, Switzerland is the Swiss Paying Agent. In Switzerland shares shall be distributed exclusively to qualified investors. The fund offering documents, articles of association and audited financial statements can be obtained free of charge from the Representative. The place of performance with respect to [shares distributed in or from Switzerland is the registered office of the Representative.*

The fund is authorized for distribution to professional investors in Hong Kong, Japan, Singapore and the UK.

By accessing information contained herein, users are deemed to be representing and warranting that they are either a Hong Kong Professional Investor or are observing the applicable laws and regulations of their relevant jurisdictions.

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