Foreign investors sniff value in Vietnam

By Ben Bland in Hanoi

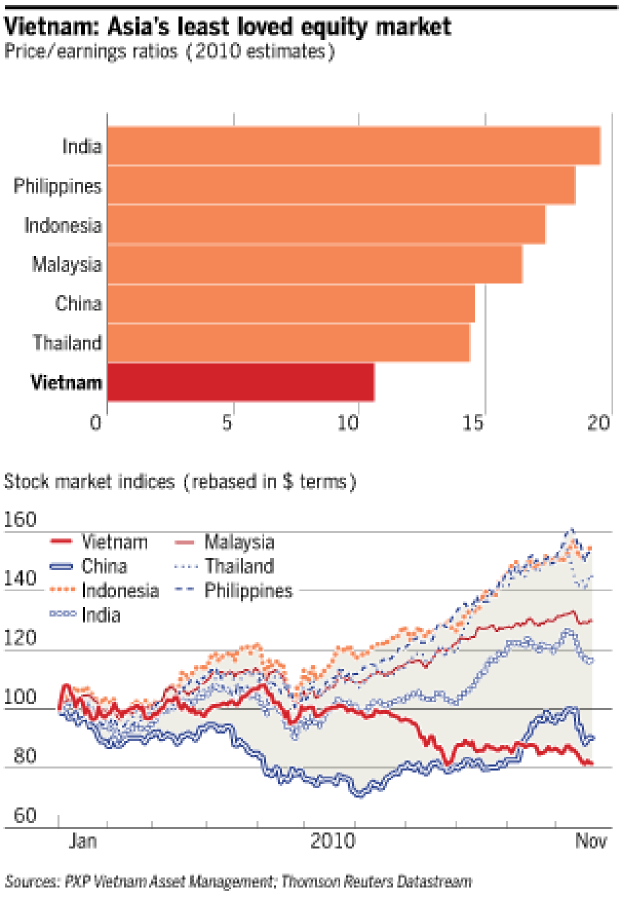
While stock markets across Asia have been boosted by hot money inflows from European and American investors, Vietnam's nascent stock market has been passed by.

The benchmark VN index has fallen 14 per cent this year amid concerns about inflation, a weakening currency and Vietnam's sizeable trade deficit. It is still 63 per cent below its 2007 record high.

Foreign investors have largely shunned the country after the pre-crisis Vietnamese investment bubble blew up in late 2007 as inflation started to spiral and turmoil in global financial markets began to sap risk appetite.

But with valuations among the cheapest in Asia and Vietnam's economy forecast to grow at the fastest pace in the region after China and India, foreign investors are starting to look at the market again and ask if the discount is really deserved.

"Now that valuations have risen significantly elsewhere . . . Vietnam is back on the radar," HSBC argues in a note that urges investors to "take a fresh look" at Vietnamese stocks.



That is a view echoed by Vietnam-based fund managers such as PXP Asset Management, Dragon Capital and VinaCapital, which manage a range of international Vietnam funds listed in London and Dublin. All three companies say that interest from international investors in Europe, the US and Asia has picked up noticeably over the past few months.

Foreign investors have been net buyers of more than $400m of shares this year on the main Ho Chi Minh Stock Exchange, according to local brokers. Daily trading is still dominated by Vietnamese retail investors. But foreign trading volumes have picked up over the past couple of months, says Kevin Snowball, chief executive of PXP Asset Management, from a two-year average of about 5 per cent of daily volumes to about 15 to 20 per cent.

That growth has been driven by a realisation that Vietnamese shares are too cheap relative to their south-east Asian peers, he believes.

Vietnam's market is trading on a 2010 forecast price-to-earnings ratio of 10.6 times, compared with 14.4 times for Thailand, 17.4 times for Indonesia and 18.6 times for the Philippines, according to data from PXP Asset Management. Yet average growth in earnings per share at Vietnamese companies, forecast at 27 per cent for this year, is ahead of all of these countries. "The market has come down a lot but earnings have been holding up," says Bill Stoops, chief investment officer of Dragon Capital.

Historically, too, Vietnam looks cheap, with the market having traded in a range of 8 times to 35 times earnings since it achieved significant scale around 2006. Adrian Cundy, head of research at VinaSecurities, VinaCapital's brokerage arm, says that the valuation gap between Vietnamese and other Asian equities looks attractive.

But he thinks the hot money is bypassing Vietnam for several reasons. "I don't see how you're going to have a vibrant institutional investor base until there's a more open capital account, foreign exchange reserves recover and it becomes easier for foreign investors to open trading accounts here."

The small size of Vietnam's equity market – there are only eight stocks with a market capitalisation of more than $1bn – a lack of liquidity and concerns about financial reporting standards are also likely to keep many mainstream investors away from Vietnam. And that is before taking into account concerns about macro-economic stability.

Annual inflation is approaching double digits again and Vietnam's currency, the dong, which has been devalued three times against the dollar since last November, is still trading significantly below the official exchange rate in the black market.

In a report on Vietnam's market released by Asianomics, a Hong Kong-based independent research house, Gillem Tulloch argues that equities have been "cheap for a reason".

"By virtue of its size, Vietnam is not a realistic investment proposition," he says. "Even it if were, we doubt that long-term fundamental investors would find many companies that make the grade given investment ill-discipline, corporate governance abuses and a worryingly high tolerance of debt."

Vietnam-based investors such as Mr Stoops are more optimistic. But even he believes that investors need to see more evidence of the government's willingness to reform bloated state-owned enterprises, seen by many analysts as the root of macro-economic instability, before they are ready to return in numbers.