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A Possible Shift In Vietnam's Approach to COVID

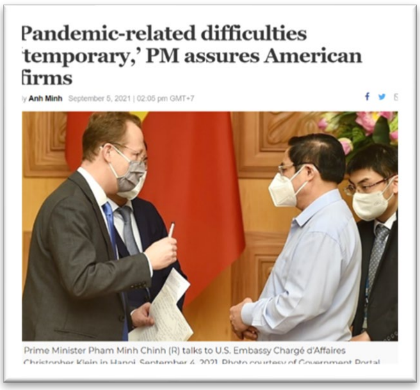
Last weekend, Vietnam's Prime Minister said that the country cannot rely on lockdowns and quarantines indefinitely to battle COVID, so reports have been circulating in the international press[1] that Vietnam will move away from a "*Zero COVID*" strategy to a "*Living with COVID*" strategy. This week, HCMC's Party Secretary said that the city "can't keep the (COVID) restrictions for long", and must "gradually reopen the economy".

Plans are reportedly now in the works to return the city closer to normal, everyday life after 15 September, and some restrictions on the movement of delivery workers within the city have already been relaxed, including to the city's "Red Zones" discussed in our last "Insights From VinaCapital" that can be found here. The city also allowed restaurants to resume accepting delivery orders this week (provided they are able to meet strict guidelines), and public health officials have declared the outbreak under control in HCMC's District 7, so it seems likely that this will be the first area in HCMC to re-open.

Finally, the World Bank and others are concerned that COVID will result in a "permanent scarring" (aka, "hysteresis") that could reduce the growth prospects of some emerging market countries for years to come.[2] However, we believe COVID will be a catalyst that ultimately *improves* Vietnam's potential GDP growth, and are encouraged by steps that many local businesses are taking to adapt to the current crisis, which is discussed below. We are also encouraged that the Government continues to respond to the concerns of foreign investors.

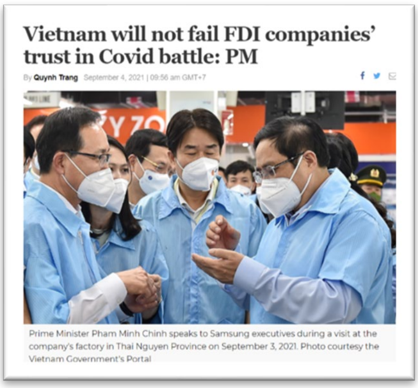
Focusing On Foreign Investors

Production disruptions in Vietnam's factories have recently attracted considerable (and unfavourable) coverage in the international business media. Last weekend, Prime Minister Chinh visited a Samsung factory where he reaffirmed the Government's commitment to protect the interests of FDI investors, and he met American business leaders, who he assured that Vietnam's pandemic-related difficulties are temporary.



Prime Minister Pham Minh Chinh (R) talks to U.S. Embassy Chargé d'Affaires Christopher Klein in Hanoi, September 4, 2021. Photo courtesy of Government Portal

The Government has consistently endeavoured to protect the interests of foreign investors given the country's dependence on foreign capital inflows to fuel economic development. The current efforts being made to enable some manufacturers to continue operating, as well as the recent relaxation of quarantine rules for foreign experts (fully vaccinated individuals approved to travel to Vietnam now need to spend just 7-days in quarantine upon arrival, making it easier for FDI companies to send employees to the country) are examples of its pro-business policy.



Prime Minister Pham Minh Chinh speaks to Samsung executives during a visit at the company's factory in Thai Nguyen Province on September 3, 2021. Photo courtesy the Vietnam Government's Portal

Finally, the efforts to support FDI companies have yielded results. Vietnam's manufacturing output dropped 4% month-on-month (m-o-m) in August, which is much less severe drop than the 15% m-o-m plunge in April 2020 when COVID first emerged and when the Manufacturing PMI plunged to a record-low of 32.7 (Vietnam's PMI stood at 40.2 in August 2021). Furthermore, industrial production (I/P) in northern Vietnam (where most of the Japanese and Korean electronics manufacturers are located) *increased* 10% yoy in August, while I/P in the southern Vietnam (where many garment, footwear, and furniture factories are located) *fell* 24% yoy.

Adapt to Survive…And Then Thrive

Modern economic history is replete with examples of countries that faced major economic challenges but then bounced back even stronger from those difficult

[1] https://www.reuters.com/world/asia-pacific/vietnams-biggest-city-proposes-sept-15-economic-restart-after-lockdown-2021-09-03/
[2] https://openknowledge.worldbank.org/handle/10986/35644

periods. In 1973, Japan's *Mainichi Shimbun* newspaper warned that the country had "*entered a catastrophic stage*," which jeopardised "*the very existence of the nation*" during the country's oil shock crisis, but this shock actually put the country on solid footing that subsequently propelled Japan's rapid growth for over 15 years.

We expect a similar phenomenon to unfold in Vietnam after the COVID crisis dissipates. Some economists believe COVID could permanently damage the economic growth prospects of many EM countries, but we believe it will likely be a catalyst that prompts Vietnam's companies to improve their business operations, and for Vietnamese policy makers to resume stalled economic reforms that will further boost the country's sustainable GDP growth potential (Side note: we are referring to reforms that would boost the country's structural economic growth potential over a long-term horizon).

The stock market seems to believe that Vietnam's economy will "bounce back stronger", evidenced by the fact that the VN-Index is up nearly 10% since April 27th, when the Delta variant first hit Vietnam. Furthermore, the stock prices of companies that have adapted to the current situation have fared even better. VinaCapital's portfolio managers and research analysts identified such companies early on when the outbreak first emerged. Our VVF UCITS fund has increased 37% YTD as of end-August versus a 21% increase in the VN Index.

Adapting Anecdotes

We have been impressed by measures taken by local companies to sustain their business operations during the pandemic. In our previous reports, we highlighted FDI manufacturing companies' efforts to continue producing their products. Below are a few examples of Vietnamese companies' efforts to continue serving local consumers:

- Local banks have started offering a much wider range of services online, including opening accounts, selling wealth management products, and even making loan approvals (albeit for small loans).

- Mobile World Group's grocery subsidiary is now delivering over 50,000 orders a day, a five-fold surge over previous volumes because many people are restricted from going to the supermarket.

- Some real estate companies are now offering virtual tours of their new projects, and one savvy industrial park developer offers prospective tenants in Japan, Korea, and elsewhere an interactive, on-line tour of its industrial parks that can be seen here.

These digitalization examples may be passé to some, given the online experiences of consumers in the developed world, but they illustrate: 1) the quick adoption of new business practices by Vietnamese businesses across the country, and 2) how the well-known "technology leap frog" effect is another factor boosting Vietnam's long-term growth prospects (i.e., developing countries can accelerate economic growth by implementing advanced technologies directly and skipping over legacy technologies and business practices).

Further to that last point, the proportion of Vietnamese companies using digital platforms and social media to sell their products has surged from below 50% in mid-2020 to nearly 75% at the beginning of this year, according to a survey by the World Bank. Vietnamese consumers had *already* enthusiastically embraced e-commerce before COVID emerged, so local companies that have adopted e-commerce will benefit long after the crisis passes. Note that over half of Vietnamese consumers shopped online pre-COVID, and over 80% of Vietnam's 25–30-year-old cohort shops online, according to a report JP Morgan published last year[3].

Finally, Vietnam's Government aims to increase the contribution of the digital economy from 5% of GDP to 33% by 2030. COVID has been extremely challenging for Vietnam in many ways, and the human costs of the epidemic for the country have been high, but COVID is also propelling the development of the country's digital economy, as it has in many other countries around the world.

Summary

The current COVID crisis is very challenging for Vietnam, but we are encouraged by the emerging details of the Government's re-opening plan, by the Government's avowed support for foreign investors, and by the fact that many local companies are adapting reasonably well to the current situation. All of this gives us confidence that the country's economy will ultimately come out of the current COVID crisis stronger.

[3] https://www.jpmorgan.com/merchant-services/insights/reports/vietnam-2020

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