Notes from the road: Vietnam and the Philippines

At LGM, travel plays a key role in the research and portfolio management process. There is nothing like meeting a company's management on their own turf to get a much rounder and ultimately deeper perspective on how the business is run. This takes on an even greater relevance in emerging market countries where we deal with an extremely diverse set of economies, societies and people.

Most recently we visited what many see as two of Asia's rising stars, Vietnam and the Philippines. Both are currently enjoying world-beating GDP growth rates of 6.2% and 6.9% respectively, and with income per capita of less than three thousand dollars in both countries, the scope for significant further growth is clearly enormous.

A stable government...

In the past year or so we've seen and read much about the Philippines' "colorful" president, Rodrigo Duterte, and he certainly remains as controversial as ever. During our visit he proudly claimed that, as part of his war on drugs, an average of nine people had been killed each day since he became president. He also said that the opposition leader should do everyone a favor by committing suicide and that he would never visit the "lousy" U.S. Despite this — or perhaps because of this — Duterte remains hugely popular, which was abundantly clear from the locals we spoke with. Indeed, Duterte's personal approval rating has been consistently above 80%. Somewhat to our surprise, this optimism and support was also shared by many of the companies that we met. The general view appears to be that while Duterte is focussed on combatting drugs, terrorism and corruption, the management of economic policy has largely been outsourced to highly competent and effective technocrats. It's all very much business as usual as far as the corporate world is concerned.

LGM Investments

Rishikesh Patel
Fund Manager

Anders Heegaard
Research Analyst

Contact us

bmogam.com

bmo-global-asset-management

Company focus: Universal Robina...

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While the political landscape is undoubtedly fascinating, it was much more important for us to get to the offices of our largest investment in the Philippines, the snack foods and beverage maker, Universal Robina (URC). We met with the owner-CEO, Mr. Lance Gokongwei, to talk about our concerns over URC's recent acquisition strategy, the competitive environment in general and also the lingering problems caused by product recalls in Vietnam last year. We came away greatly reassured, even though the competitive environment is likely to remain challenging for the foreseeable future, especially in the coffee business. The CEO clearly acknowledges that URC has made mistakes, especially by overpaying for the recent acquisition of Griffin's in New Zealand and by taking their eye off the ball in the domestic market. The strategy now is to focus on core competencies, to rationalize SKUs and to cut costs. Further acquisitions have been ruled out. URC is not out of the woods yet, but we are encouraged that management has faced up to its mistakes and learned valuable lessons. With URC's market-leading brands in underpenetrated categories, superior distribution, robust balance sheet and great management team, we remain confident in the long-term outlook for this business.

The past to the present...

Vietnam's development record over the past 30 years has been quite remarkable. Having visited the country numerous times in the past decade, it has been fascinating to watch the transition from central planning to what is now largely a market driven economy. One sometimes forgets that Vietnam is still run by a communist government.

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Consumer sentiment was positive and clearly on view, with many western brands like McDonald's and Starbucks (and others) buzzing with eager customers. While this is all very encouraging, as long-term investors it really doesn't mean a whole lot if we cannot find good companies to invest in. And this is where some problems arise.

As we mentioned, the economic landscape is looking pretty rosy and Vietnam certainly ticks all the boxes as a "true emerging economy", but the main problem is that we don't find a huge number of genuinely investable companies on offer. This partly arises from the lack of choice in the equity market (where there simply aren't that many listed companies), but the real culprit is the lack of quality management.

However, thankfully there are always exceptions to the rule and Vietnam Dairy Products (Vinamilk) is certainly a good example of this — despite the government continuing to own almost 40% of the shares. LGM has been invested in Vinamilk for many years and the company has consistently impressed. It is the leading diary producer in Vietnam; it has market leading brands and runs an extremely tight ship in terms of cost efficiency and capital allocation. On this trip we had the opportunity to visit a new production facility just outside Ho Chi Minh City. This was a highly automated, state of the art facility that would stand comparison with similar plants anywhere in the world. We were given a tour by the plant manager and it was interesting to see how eager he was to discuss "payback periods" on machinery and the benefits of automation and robotics. This was not the usual conversation you get from plant managers in relatively remote facilities in the still less developed part of the emerging market universe.

We left each market with strong confidence in the companies where we are invested and also in the growth outlook for both countries. While progress has certainly been impressive, there still remain substantial challenges to future development, none more so than the idiosyncrasies of the ruling entities in both countries.

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