<u>Vietnam is a Player in the PPE market…but be careful</u>

Philip Ziter

Russin & Vecchi

Not all economic sectors have suffered from COVID-19 -- indeed some have prospered because of it. The global demand for personal protective equipment ("**PPE**"), which includes facemasks and medical examination gloves, has surged.

Companies that were already producing or trading PPE were perfectly positioned. Demand has far outstripped supply, causing prices to rise and a flood of newcomers to enter the space. The dramatic increase in cross-border trade of PPE has triggered a flood of opportunities for buyers, sellers, and intermediaries. But to navigate the complexities of the opportunity requires caution.

In this piece we use the terms "Sellers" and "Buyers" in their normal sense. But there are some caveats, as the manufacturer is not always the Seller. A Seller is often a separate entity, which has a commercial relationship with the manufacturer. The Buyer is the party in interest. However, it is the norm that both Buyers and Sellers often work through "intermediaries". Intermediaries can be "agents", who act specifically on behalf of a Buyer or Seller, or "brokers" who act as independent middlemen. Brokers and agents may provide a legitimate service, but the objective is generally for the Buyer and Seller to deal directly with each other. This, however, is not always possible.

Vietnam is an established player of relatively modest size and experience when compared to more developed suppliers like China, Malaysia, Thailand. Masks of various types (eg, 3 and 4 ply surgical masks) have long been produced in Vietnam in lesser quantities. But now, even garment factories have been repurposed to produce cloth masks and slightly more complex items like medical gowns.

Nitrile gloves are manufactured by a number of factories but only two factories appear capable of producing relatively large volumes. The biggest one is government owned, which adds an additional layer of complexity. New, much smaller factories have begun to produce modest numbers of gloves for export.

Large orders are often not in stock, need to be manufactured, and then delivered over time. This means that there are waiting times and risks. In some limited cases, pre-manufactured inventory can be delivered from existing stock held in a warehouse. In the case of high demand products, for example nitrile gloves, available stock inventories are far scarcer. This has created a high risk that nitrile gloves which are immediately available for shipment may be fake or may not meet safety requirements.

Manufacturers need to have certifications which will permit the products to be imported into and sold in various countries (eg, CE, FDA, EN 455, EN 374-5, 510K, etc). Certification must be verified, and this can be a challenge for new factories.

A question the Buyer has to answer is, if the products need to be manufactured, does the manufacturer have the capacity? A clear answer is often not easy. Many factories don't work directly with the Buyer, and instead will work only through an agent it has vetted. Many agents are new and do not have a track record. A further complication is that many manufacturers do not allow pre-deal verification visits to the factory. This is particularly true for gloves and is especially true of the government owned factory.

The Seller, which may or may not be the manufacturer, interfaces with the Buyer, its agent, or independent brokers, and the transaction is usually between those entities. New Sellers are more difficult for the Buyer to vet.

As the transaction, is typically driven by intermediaries, brokers on both sides of the transaction act as facilitators and are paid a fee for their services. Brokers can be assets or liabilities to a transaction. On the one hand they can be experienced, have the trust of the principals, and have a true commercial impact. On the other hand they can be inexperienced, unrealistic in their expectation for commissions, or even fraudulent.

Broker's great fear is that the Buyer or its agent will circumvent it and deal with the factory directly, or with a Seller they have not introduced. Thus, the Broker's statements are not always reliable, and they may block access to the Seller/Manufacturer. This makes due diligence particularly challenging when Buyers are attempting to vet the supplier.

What gives pause, when the Manufacturer is not the Seller, is that while the Manufacturer often has substance and can perform, the Seller and/or Broker(s) may have no assets, may have no verifiable track record, and so cannot be easily evaluated.

Payment: For smaller orders the Seller normally expects to be paid via wire ("**TT**") -- usually 30-50% upon placement of the order and the balance upon delivery (ie, delivery according to the incoterms stated in the Sale and Purchase Agreement – EXW, FOB, CIF, etc). Escrows are becoming more acceptable, but, when acceptable, Sellers don't want complicated sign-off and usually want sign-off and release before the goods are boarded.

Letters of Credit are perfect for this sort of fact situation, but Sellers seem only to allow them for larger orders, and generally only with international banks. Documentary L/Cs follow a general set of rules published by the International Chamber of Commerce (**"ICC"**) [Uniform Customs & Practice (UCP600)]. Payment options may be evolving but the fact remains that this is a Seller's market. Increasingly limited supply capacity and increasing cost of raw manufacturing materials mean Sellers can, and do, turn down deals if Buyers are not willing to work under the desired terms, which often include a deposit.

Sellers often also require a buyer to provide proof of funds ("**POF**") at the letter of intent ("**LOI**") stage. Generally, a bank comfort letter ("**BCL**") is requested to satisfy POF. This practice has developed as a means for manufacturers to filter out fraudsters and unqualified "Buyers". Unfortunately, this may also be abused by unscrupulous actors (eg, brokers) to gain sensitive financial information of Buyers. This information can then be used in various ways by scammers. Buyers should proceed with caution when providing sensitive information to brokers. For example, increasingly, Buyers are insisting on delivering BCLs to Sellers' attorneys, if not to the Seller itself.

Safeguards: Due diligence ("**DD**"). In any transaction with a new trading partner, a thorough DD should be done prior to signing an SPA. But as we've experienced, a DD is devilishly difficult. There is a path but it may not be perfect. Office and factory visits and inspections (if possible), meeting with brokers and/or Seller's representative, company document checks to assure it has been formed and who are the authorized signatories, certification checks, inventory verification (if possible), negotiation of contract terms, and discussion with various parties to the transaction. If possible, talk with other Buyers.

Sale and Purchase Agreements ("**SPA**") are the norm, and are recommended, even though enforceability may ultimately be problematic. At the very least, an SPA is a good checklist, providing a clear path for the transaction and is a good venue to sharpen the terms. The SPA should be carefully reviewed for its commercial terms, and to be sure it is in compliance with Vietnamese law and general Vietnam practice.

US, Vietnam, and many other countries are party to the UN Convention on Contracts for International Sale of Goods ("**CISG**") - if contracting with a counterparty in another CSIG signatory state, the CISG will apply unless expressly superseded by specific contract language.

Incoterms are part of a contract, and it is important to understand the point at which risk, and title pass (eg, EXW, FOB, etc).

Product inspection, prior to delivery, for quality and quantity, is of course critical. SGS is active in Vietnam, has experience, and can be used. Some buyers also choose to engage a second inspection company.

PPE transactions in Vietnam have unique market-specific challenges. However, the fact remains that sales of PPE from Vietnam are often completed.