

Sector note

29 Apr 2020

TEXTILE AND APPAREL (T&A)

1Q20 update: Tough time to linger

- As at 15 Apr, the year-to-date Vietnam's garment export value fell 6.0% yoy, while fibre and yarn export value slumped 6.6% yoy.
- T&A might be hit more severely in 2Q20F from demand side, in our view.
- Among T&A stocks, our top pick is STK thanks to its solid position to recover post-pandemic.

COVID-19 to hit T&A export harder since Mar 2020

From early 2020 to 15 Apr 2020, Vietnam's garment export value fell 6.0% yoy while that of fibre and yarn export dipped 6.6% yoy. According to the Vietnam Textile and Apparel Association (VITAS), since the second half of Mar, many U.S. and EU major customers have asked Vietnamese textile and apparel (T&A) enterprises to delay orders, or some even cancelled contracts. The order volume in Apr and May of T&A industry might be cut by about 70% yoy. Thus, we believe that T&A exports will be hit more severely in 2Q20F.

Gauze masks production rescues Vietnam's T&A industry

Many garment producers recently invested in producing medical and fabric gauze masks as a solution to cope with the difficult time and take advantage of the supply shortage. Several makers have received export orders worth millions of dollars, helping ease the pain from low demand for garment products. The domestic mask production capacity of the 50 biggest producers has reached nearly 200m pieces/month.

T&A enterprises posted weak 1Q20 business results

A few large enterprises have so far announced their 1Q20 business results, most of which showed lower topline and bottomline growth. We believe that the global supply chain disruptions are no longer a big deal in 2Q20 as the disease has been well-controlled in China and 90% of factories there have now resumed operation. However, Vietnam's T&A industry will still face obstacles from the demand side. In our view, domestic sales of garment manufacturers may increase thanks to the production and consumption of gauze masks, while export revenue will continue to decline in 2Q20F.

Short-term pain but long-term gain still in doubt

Lockdown measures in many countries will leave a more severe impact on Vietnam's T&A exports in 2Q20F. Therefore, we have a negative rating on the T&A sector in the short term and do not recommend investment in this period. In the long term, the EVFTA and CPTPP agreements remain the supporting factors. However, bottlenecks in fabric production and post-epidemic recovery are still the issues needed to be addressed in order to take further steps.

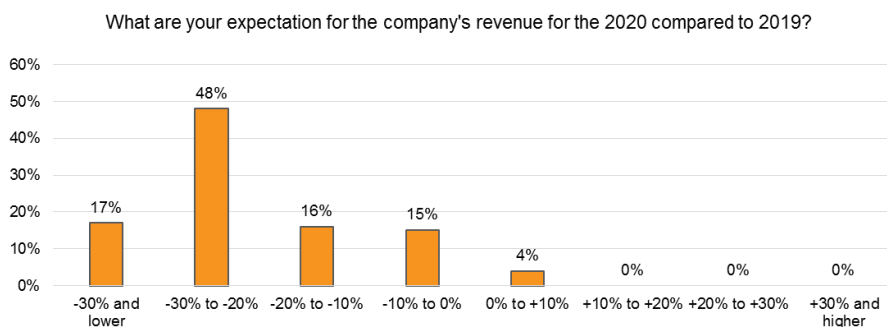
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Figure 1: Many T&A companies expected their revenue to be hit strongly in 2020F

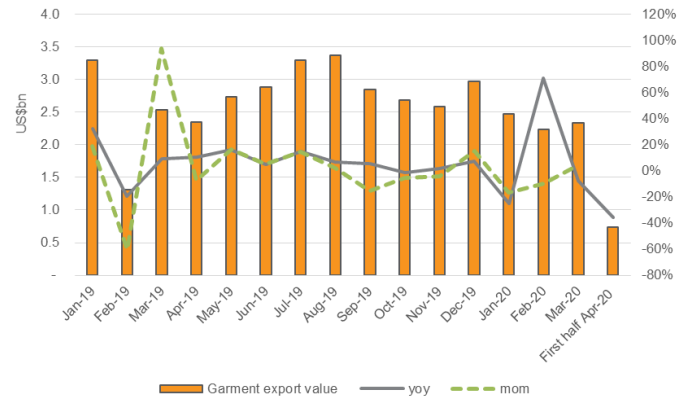


Source: VITAS (survey of about 200 medium and large Vietnamese T&A enterprises)

KEY CHARTS

Vietnam's T&A industry had a quarter of export value below the three-year average

In 1Q20, Vietnam's garment export value fell 7.7% yoy while fibre and yarn export value slipped 5.4% yoy. In the first half of Apr 2020, the impact of COVID-19 pandemic on exports has been more severe, with garment export value falling 35.4% yoy to US\$739m.



Source: CUSTOMS, VNDIRECT RESEARCH

Fabric import value in Mar 2020 soared 50.6% from Feb

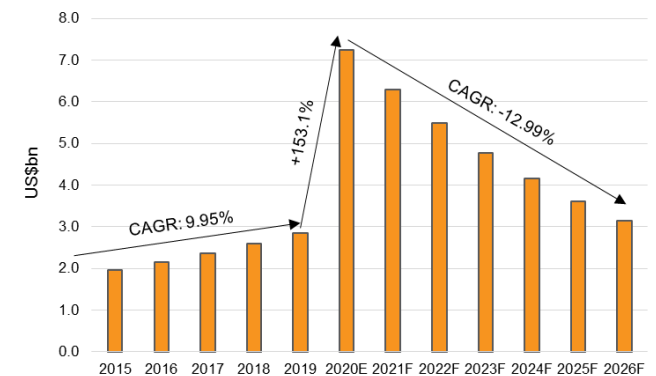
As 60% of the fabric used for Vietnam's domestic garment production is imported from China, the domestic fabric demand jumped sharply in 1Q20 due to China's production disruptions. In addition, increased production of face masks during the pandemic has also resulted in higher fabric demand. In particular, Mar 2020 fabric import value soared 50.6% from Feb to US\$1.07bn.



Source: CUSTOMS, VNDIRECT RESEARCH

Global market size of gauze masks in 2015-26F (US\$bn)

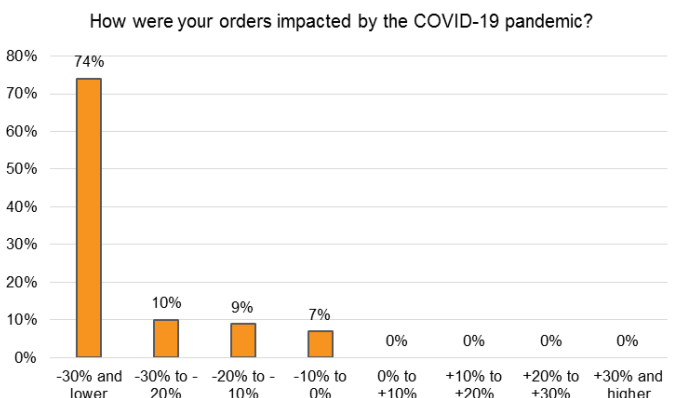
The pandemic has created a huge demand for medical and fabric masks, resulted in a supply shortage globally. In Mar 2020, the Vietnam National Textile and Garment Group (VGT) and its members delivered an estimated 15m of anti-bacterial masks to the market while maintaining a daily output of nearly 35 tonnes of anti-bacterial knitted fabric, contributing to the prevention of the spread of the pandemic. Apart from Vinatex, other textile enterprises nationwide have also actively participated in mask production, helping ensure domestic supply.



Source: QYResearch 2020

Percentage difference of orders gained/lost since the start of COVID-19 outbreak

Developed countries where most of Vietnam's T&A industry orders come from including the United States (accounting for 50% of total export turnover) and the EU market (accounting for 12% of total export turnover) have been swept up in the pandemic crisis with a rapidly increasing rate of confirmed infections and deaths. U.S. and EU governments have thus temporarily closed their borders and enforced restraining orders.



Source: Survey by VITAS

1Q20 earnings update of listed T&A enterprises

A few large enterprises have so far announced their 1Q20 business results, most of which show lower topline and bottomline.

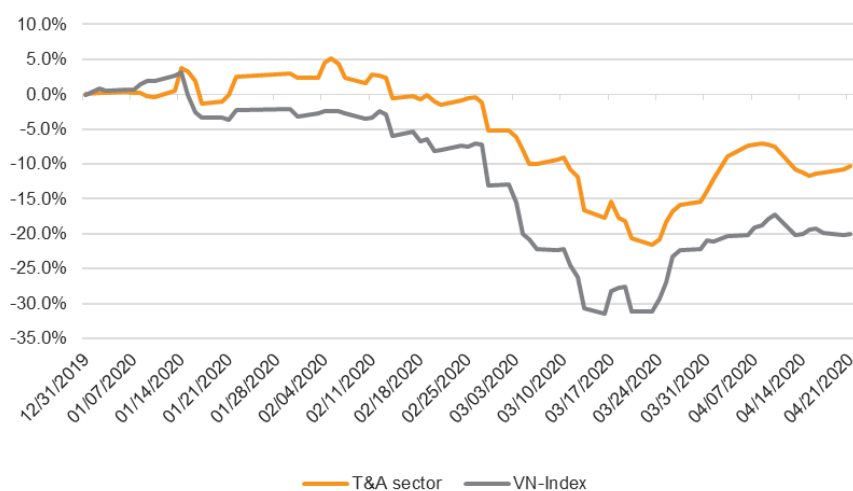
Figure 2: 1Q20 business results of large listed Vietnamese T&A enterprises as at 29 Apr 2020

	Revenue (VNDbn)			Net profit (VNDbn)			Gross profit margin			vs. our FY20F forecasts	
	1Q19	1Q20	% yoy	1Q19	1Q20	% yoy	1Q19	1Q20	Change yoy	Revenue	Net profit
TCM	978	790	-19.2%	43	34	-20.9%	14.8%	14.4%	-0.4 %pt	19.4%	11.3%
TNG	806	773	-4.1%	37	34	-10.0%	18.7%	18.8%	+0.1 %pt	N/A	N/A
STK	605	617	1.9%	52	52	0.3%	13.8%	15.4%	+1.6 %pt	25.5%	20.7%
GIL	545	722	32.4%	32	43	32.2%	17.2%	16.0%	-1.2 %pt	N/A	N/A
HSM	585	390	-33.4%	(4)	6	0.0%	4.8%	10.6%	+5.8 %pt	N/A	N/A
HTG	1,081	978	-9.5%	24	26	6.9%	7.5%	9.1%	+1.6 %pt	N/A	N/A
M10	712	772	8.3%	16	11	-32.0%	15.9%	12.9%	-3.0 %pt	N/A	N/A
VGG	1,726	1,475	-14.5%	88	(21)	0.0%	13.6%	8.3%	-5.3 %pt	N/A	N/A

Source: VND Research, Bloomberg

As at 29 Apr 2020, the stock price of T&A sector fell 10.3% ytd but still outperformed the VN-Index (-20.0% ytd) as many large-cap stocks in other industries had more steep drops.

Figure 3: T&A sector price outperformed VN-Index in 2020



Source: Fiipro, VNDIRECT Research

Figure 4: T&A peer comparison (as at 29 Apr 2019)

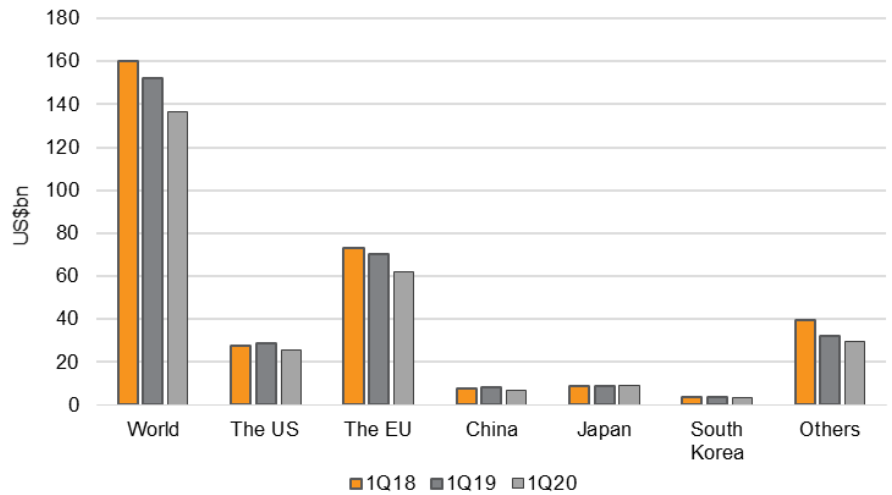
Company	Bloomberg Ticker	Target price (local curr)	Market Cap (US\$m)	TTM NPAT growth (%)	TTM EPS growth (%)	TTM ROA (%)	TTM ROE (%)	D/E (x)	TTM P/E (x)	TTM P/B (x)	
Synthetic fiber manufacturers											
Century Synthetic Fiber	STK VN	ADD	22,400	51.3	12.8%	18.0%	10.2%	21.5%	0.6	5.6	1.1
Apparel and garment manufacturers											
Thanh Cong Textile Garment	TCM VN	ADD	27,700	38.1	-18.4%	-16.7%	7.0%	13.7%	0.7	5.1	0.6
Song Hong Garment	MSH VN	ADD	51,600	71.3	21.6%	-10.9%	17.6%	42.9%	0.4	3.7	1.4
Viet Tien Garment	VGG VN	N/A	N/A	76.2	-11.0%	-10.9%	10.1%	24.0%	0.0	5.7	1.1
TNG Inv'm't and Trading	TNG VN	N/A	N/A	34.2	15.6%	22.1%	7.2%	24.1%	1.3	3.4	0.8
Viet Thang Corp.	TVT VN	N/A	N/A	18.4	-11.9%	-11.1%	5.3%	13.1%	1.3	5.6	0.8
Garmex Saigon	GMC VN	N/A	N/A	18.7	-13.6%	10.3%	10.2%	24.2%	0.5	3.0	0.7
Nha Be Garment	MNB VN	N/A	N/A	N/A	12.0%	15.5%	1.8%	15.6%	4.7	N/A	N/A
Average				42.8	-0.8%	-0.3%	8.5%	22.5%	1.3	4.4	0.9
Median				36.1	-11.0%	-10.9%	7.2%	24.0%	0.7	4.4	0.8

Source: VND Research, Bloomberg

A sharp drop in T&A orders since the start of the year

Global T&A industry has experienced a difficult year in 2019 due to the U.S.-China trade war. While the wound has yet to heal, another pain called COVID-19 emerged. Its impact turned out to be greater than that of the trade war, as the global T&A supply chain was interrupted and demand fell sharply in 1Q20. Accordingly, the world's import turnover in 1Q20 decreased 10.3% yoy, more than double the 4.9% yoy fall in 1Q19.

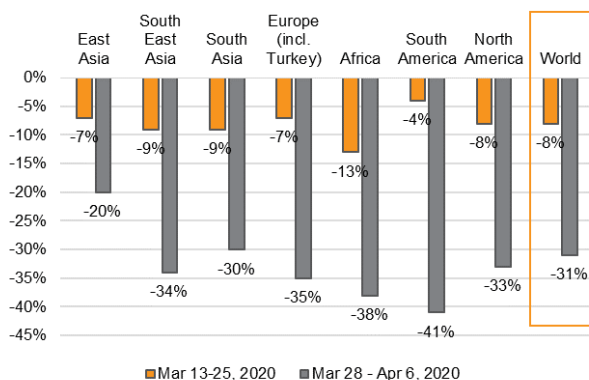
Figure 5: T&A import value of major countries in 1Q18-2020 (US\$bn)



Source: VITAS

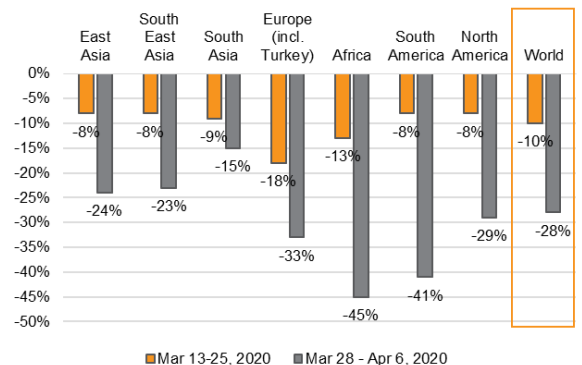
On 13-15 Mar 2020, the International Textile Manufacturers' Federation (ITMF) conducted the first survey on the global T&A value chain among pandemic-hit members. A total of 34 companies worldwide, along with two national T&A associations and hundreds of people participated in the survey. Another survey took place from 28 Mar to 6 Apr 2020, joined by 700 companies around the world. The surveys found the pandemic leaves a devastating impact on the global T&A industry.

Figure 6: COVID-19's impact on T&A orders by region in 2020F (% yoy)



Source: ITMF Survey (28 Mar-6 Apr, 2020)

Figure 7: COVID-19's impact on T&A turnover by region in 2020F (% yoy)



Source: ITMF Survey (28 Mar-6 Apr, 2020)

According to VITAS, from the second half of Mar, many U.S. and EU major customers have asked Vietnamese T&A enterprises to delay orders, or some have even cancelled contracts. The volume of orders in Apr and May of T&A industry will be reduced by about 70%; new orders from Jun onwards have not been negotiated and any recovery in the number of orders by end-2020F will

be very slow. Thus, we believe that the 2Q20F business results of Vietnam's T&A enterprises will show more severe impacts due to the low demand amid the pandemic.

Masks production rescues Vietnam's T&A industry

According to Ministry of Industry and Trade statistics on 50 enterprises, the domestic mask production capacity has reached 8m pieces/day, or nearly 200m pieces/month. On the national scale, the capacity will be much greater.

Gauze mask is a product that does not require a lot of investment. Most of the existing factories, equipment and workers in Vietnam's garment industry can make masks. The antibacterial fabric material used to make gauze masks can be produced domestically or imported from China or South Korea without difficulty. Therefore, Vietnam's mask production capacity is huge. After meeting domestic demand, the product can be exported, making the country the world's new mask production hub.

Among garment manufacturers, VGT (VGT VN, Not rated, CP: VND7,700), TNG (TNG VN, Not rated, CP: VND12,200), M10 (M10 VN, Not rated, CP: VND21,000), MSH (MSH VN, Add, TP: VND51,600), TCM (TCM VN, Add, TP: VND27,700), TVT (TVT VN, Not rated, CP: VND20,500) are seizing opportunities from a huge demand for medical and fabric masks in terms of domestic consumption and export.

No short-term buffers while long-term outlook is uncertain

The disease has been well-controlled in China, and 90% of factories there have now resumed operation, restoring 85-90% of the supply of raw materials to the global T&A industry. Thus, global supply chain disruptions are no longer a big deal. However, the alarming spread of the pandemic in the United States and EU countries has led to a sharp drop in the demand for textile and garment products in these markets. The pandemic has constrained global retail growth.

Lockdown measures in many countries will leave a more severe impact on Vietnam's T&A exports in 2Q20F. Therefore, we have a negative rating on the T&A sector in the short term and do not recommend investment in this period.

In the long term, the EVFTA and CPTPP agreements remain the supporting factors. However, bottlenecks in fabric production and the post-epidemic recovery are still the issues needed to be addressed in order to take further steps.

Our stock pick is STK thanks to its improving yarn product mix with higher contribution of recycled yarn. Amid COVID-19, the company's raw material supply is not affected by China's production disruption as it imports materials from the United States, Thailand, or Taiwan. STK's risk may come from a declining production demand from garment companies. However, low oil prices and increasing demand for yarns to produce gauze masks and medical protective equipment may help STK maintain its operation better than other garment enterprises. In our view, STK may see the strongest post-pandemic rebound among T&A companies.

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RECOMMENDATION FRAMEWORK

Stock Ratings

Definition:

Add	The stock's total return is expected to reach 15% or higher over the next 12 months.
Hold	The stock's total return is expected to be between negative 10% and positive 15% over the next 12 months.
Reduce	The stock's total return is expected to fall below negative 10% over the next 12 months.

The total expected return of a stock is defined as the sum of the: (i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.

Sector Ratings

Definition:

Overweight	An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation.
Neutral	A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
Underweight	An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

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