Sector note

12 Aug 2021

Textile & Garment (T&G)

Challenges to blur the outlook

- 2Q21 aggregated net profit (NP) of listed T&G companies returned to pre-pandemic level, surging 141.7% yoy and 46% vs. 2Q19.
- We see challenges to blur the industry outlook, including manufacturing disruption and rising administration cost due to the current outbreak.
- Our top pick is STK while MSH is on the watchlist.

Earnings to grow robustly in 2Q21

Vietnam's T&G export turnover climbed 24.6% yoy in 2Q21, even 7.4% higher than pre-pandemic level (2Q19), thanks to increasing demand of Vietnam's primary export markets, include the U.S. (+42% yoy) and E.U (+18% yoy). Based on our estimates, 2Q21 aggregated revenue of listed T&G companies jumped 22.1% yoy, while 2Q21 aggregated NP soared 141.7% yoy driven by: 1) low base 2Q20 as production disrupted for a few weeks during the first wave outbreak, 2) better product mix (recycled yarns, bed mats), and 3) increasing in FOB orders (shifting orders from epidemic-affected countries to Vietnam).

Riding on the demand surge in U.S and E.U. market

The U.S. and E.U. consumers have shown a solid pent-up demand after lockdown. The U.S.'s T&G import turnover in 1H21 increased by 31.16% yoy to US$50.6bn, of which import turnover for apparel grew 26.9% *(Source: OTEXA)*. In addition, according to the General Department of Vietnam Customs (GDVC), E.U.'s T&G import turnover from Vietnam in May-21 and Jun-21 soared 11.9% yoy and 21% yoy, respectively thanks to reopening economy.

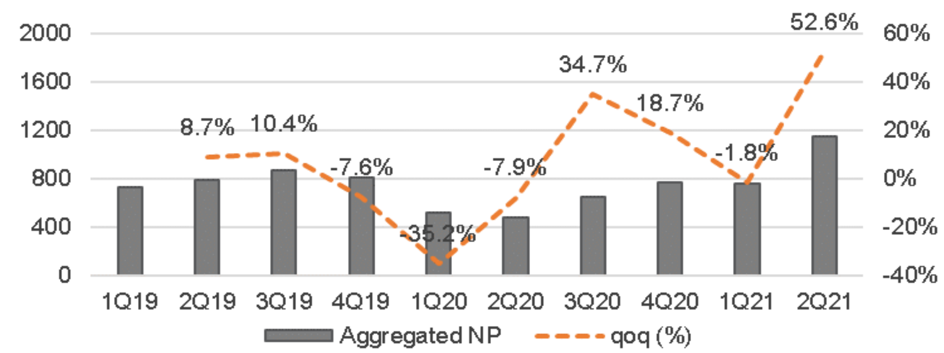
2H21 outlook will be dictated by the current Covid-19 wave

The COVID-19 outbreak in the South region could disrupt supply chains again as companies cannot deliver raw materials and ensure timely deliveries due to a lack of human resources. We see that T&G companies with factories in the South area are hardest hit, like **VGT, TCM, and GMC**. If the current situation lasts for several weeks, we forecast that additional expenses for meals, accommodation and Covid-19 vaccination for employees account for 10% of T&G companies' s G&A expense in FY21F. VITAS forecast in the optimistic scenario, if the Covid-19 is under control by the end of Aug-21, T&G export turnover in 2021 may only reach US$33bn (-6% yoy).

STK is our stock pick

We like STK regarding: 1) strong revenue growth from recycled yarn in FY21-23F; 2) capacity expansion plan – doubling capacity in 2025F and 3) gain more market share from the U.S. market thanks to the low preliminary anti-dumping duty.

Figure 1: Quarterly aggregated net profit of listed T&G companies (Unit: VNDbn)



SOURCES: Vinatex, VND RESEARCH

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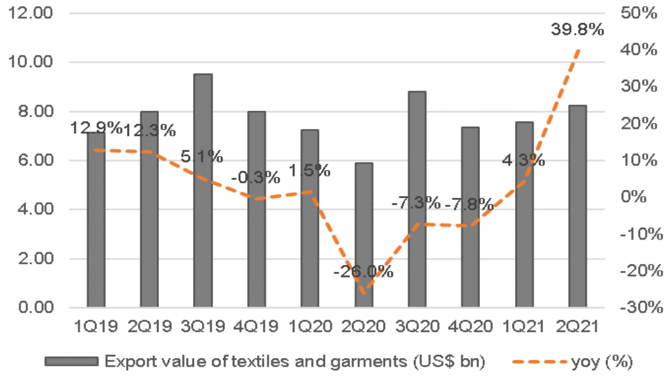
VIETNAM TEXTTILE & GARMENT SNAPSHOT IN 1H21

Vietnam's textile and garments export value

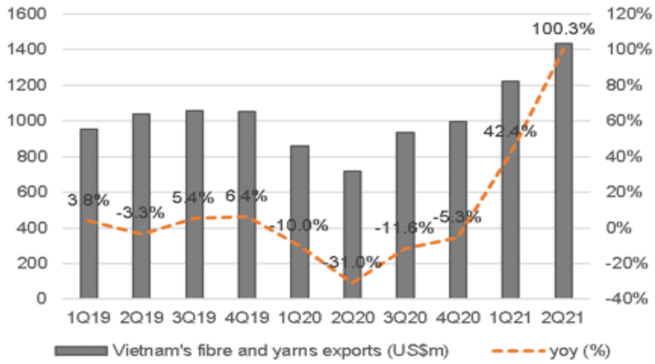
In 2Q21, the garment and textile export turnover returned to pre-pandemic level thanks to sales volume recovery from Vietnam's main export market such as U.S. and E.U. As a result, fabrics and garment export value in 2Q21 grew 39% yoy to US$8.2bn. In which, fabric exports reached US$1.3bn, accounting for 7.6% of the total T&G export turnover (+33.5% yoy). Overall, the total export T&G value in 7M21 increased by 14.1% yoy, to US$18.6bn, fulfilling 47.6% of the Vietnam government's guidance for 2021F (US$39bn).



Sources: MOIT, VNDIRECT RESEARCH

Vietnam's fiber and yarn export value

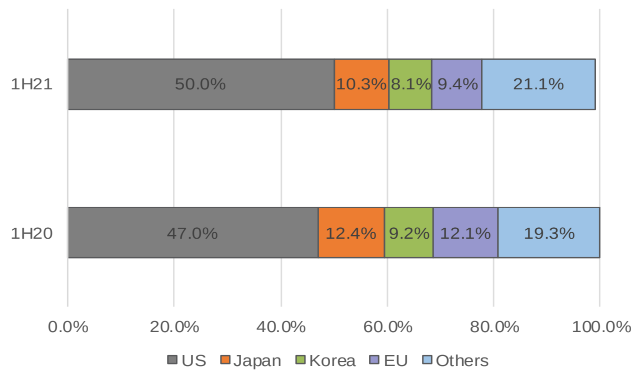
Yarn prices in 2Q21 soared by 28.8% yoy due to the depletion of yarn inventories in China, along with the U.S. and E.U.'s ban on products derived from Xinjiang cotton, causing increased demand for yarn outside China. As a results, yarn and fibers export turnover rebound in 2Q21 with 100.3% yoy growth to US$1,4bn. Notably, Vietnam's polyester filament yarn export value in 1H21 recorded US$225.1m (+40.0% yoy).



Sources: MOIT, VNDIRECT RESEARCH

T&G export destination in 1H21

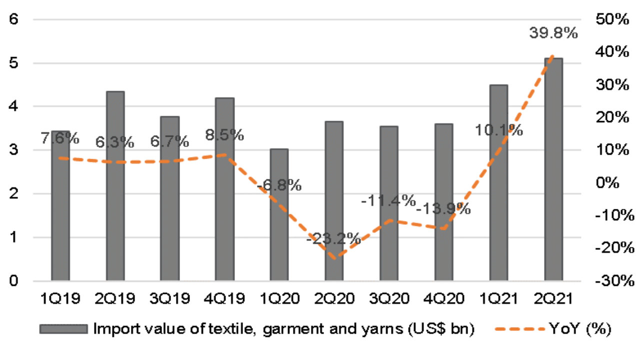
According to (GDVC), regarding export mix by geographic regions in 1H21, The US remained the largest importer of Vietnam T&G products with an import value of US$7.6bn (+ 23% yoy, 48.0% of Vietnam's textile and garment exporting value). 1H21 exporting to E.U. markets reached US$1.51bn, increasing 14.5% yoy. Whereas, exporting to Japan and Korea markets declined 10.3% yoy and 8.1% yoy, respectively, to US$1.57bn and US$1.24bn in 6M21.



Sources: GDVC, VNDIRECT RESEARCH

Vietnam's yarn, textile and garment import value

According to MOIT, the total import value of T&G in 2Q21 reached US$5.11bn (+39.8% yoy) thanks to the recovery sales volume of T&G businesses in 2H21 (most T&G companies have full order until end of 2021). In which, China is still the main import market of Vietnam, accounting for 49.0% T&G import value. We expect Vietnam's T&G import turnover maintain the growth momentum in 2H21 as traditional order will rebound in 2022F thanks to rapidly vaccination roll out in the Vietnam's main export markets.



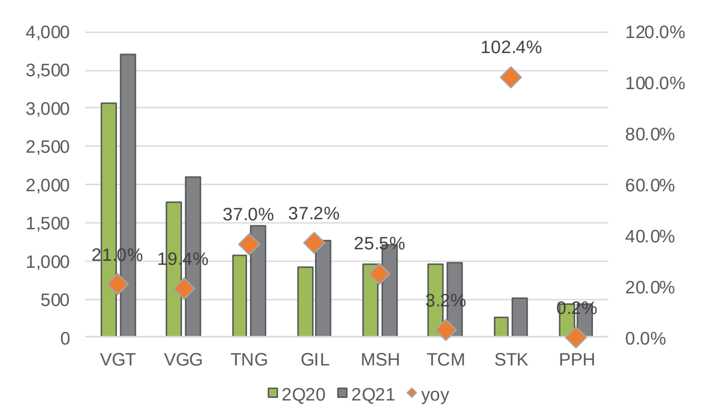
Sources: MOIT, VNDIRECT RESEARCH

CHALLENGES TO BLUR THE OUTLOOK

Earnings to grow robustly in 1H21

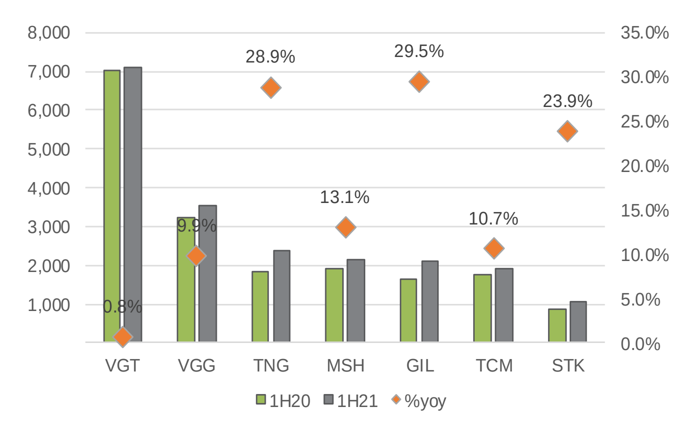
Based on our estimate, 2Q21 aggregated revenue of listed T&G companies soared 22.1% yoy mainly driven by strong demand from the U.S. and E.U. market, much higher than a decrease of 7.6% yoy in 1Q21. Consequently, 1H21 aggregated revenue of listed T&G companies increased 7.3% yoy but slightly fell 12.3% vs 1H19. TNG and GIL posted strong revenue growths in 1H21 with 28.9% yoy and 29.5% yoy, respectively as these manufacturers quickly grabbed orders shifting from competitor countries to Vietnam.

Figure 6: The revenue of T&G listed companies in 2Q21 (VNDbn)



Sources: Fiinpro, VNDIRECT RESEARCH

Figure 7: Most of T&G companies showed a solid revenue growth in 1H21 (VNDbn)



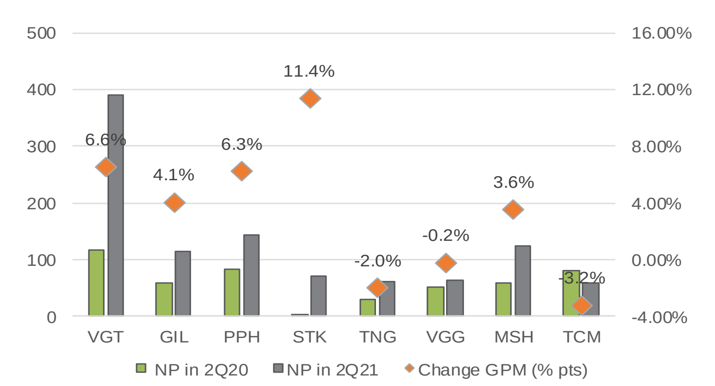
Sources: Fiinpro, VNDIRECT RESEARCH

We see gross margin improvement across sector 1H21. To be specified, STK's gross margin inched up 11.4% pts yoy to 19.5% in 1H21 thanks to 1) larger contribution with higher margin recycled yarn (56% of 1H21 revenue vs 38% of 1H20). VGT's 1H21 gross profit widened 6.6% pts yoy on the back of: 1) FOB orders to be shifted from Myanmar and India to Vietnam, and 2) larger contribution from yarn which delivered higher margin.

On the other hand, gross margin of TNG and TCM softened 3.8% pts yoy and 0.8% pts yoy in 1H21 due to 1) lack of gauze mask and anti-virus fabric orders and 2) increasing shipping cost from Original Designer Manufacturing (ODM) orders.

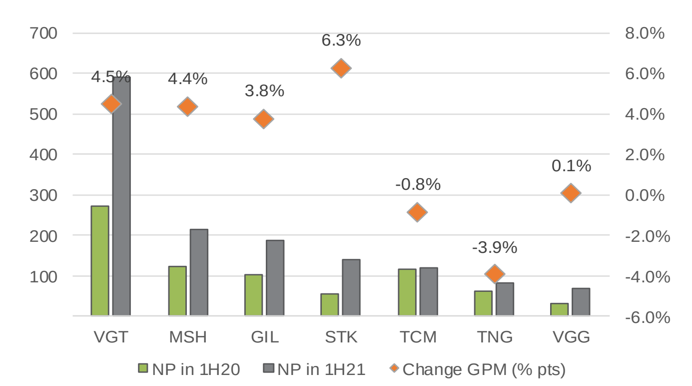
Overall, sector net profit grew 141.7% yoy in 2Q21, stronger than that of 44.6% yoy of 1Q21. 1H21 sector net profit accelerated 90% yoy and even 25.8% higher than that of 1H19.

Figure 7: 2Q21 net profit of listed T&G companies (VNDbn)



Sources: Fiinpro, VNDIRECT RESEARCH

Figure 8: Gross margin improved across the board (VNDbn)



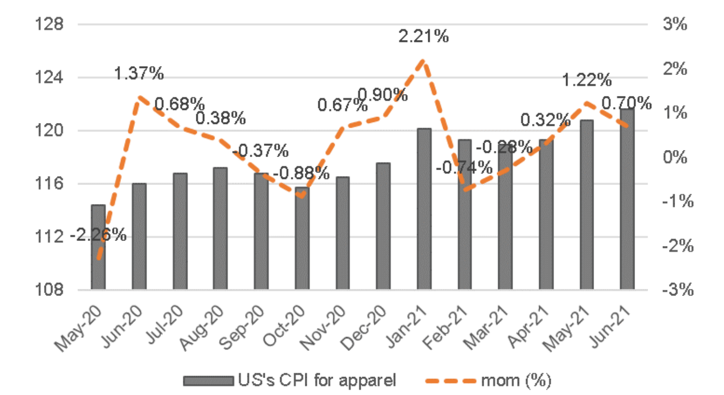
Sources: Fiinpro, VNDIRECT RESEARCH

Riding on the demand surge in U.S and E.U. market

The U.S. and E.U. consumers have shown a strong pent-up demand after lockdown. According to the Bureau of Labor Statistics (BLS), CPI for apparel advanced 1.2% mom and 0.7% mom in May-21 and June-21, respectively. Nearly half of the U.S. population has been vaccinated against COVID-19, allowing Americans to buy personal goods directly in the shop, travel and attend sporting events. As a results, The US's T&G import turnover in 1H21 increased by 31.16% yoy to US$50.6bn, in which import turnover for apparel reached US$35.3bn (+26.9% yoy).

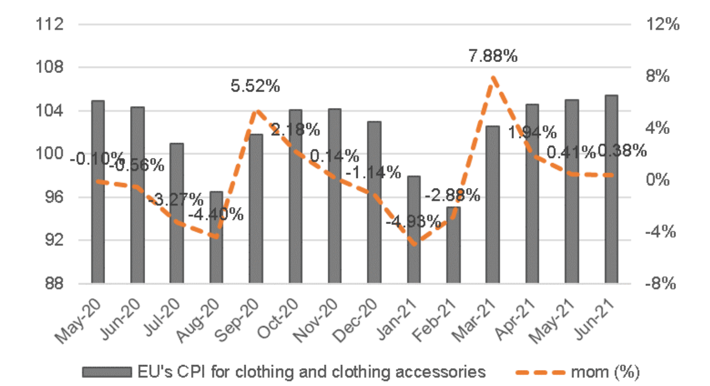
Whereas according to GDVC, E.U.'s T&G import turnover from Vietnam in May-21 and Jun-21 soared 11.9% yoy and 21% yoy, Furthermore, E.U.'s CPI for clothing and clothing accessories also rose 0.41% and 0.38% mom in May-21 and Jun-21. We expect that the U.S. and E.U. are still the two main export markets of Vietnam T&G industry in 2H21-22.

Figure 9: The U.S.'s CPI for apparel posted 121.6 pts on Jun-21 (+0.7% mom)



Sources: BLS, VNDIRECT RESEARCH

Figure 10: The E.U.'s CPI for clothing and clothing accessories increased by 0.38% mom to 105.41 pts in Jun-21



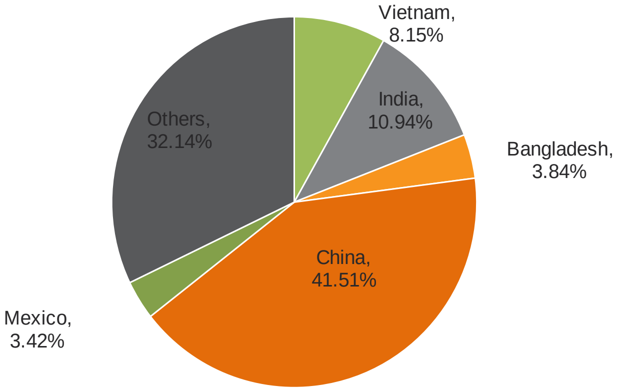
Sources: BLS, VNDIRECT RESEARCH

We see that Vietnam has a chance to grab market from competitors

Indian T&G exporters are facing the risk of losing most of their orders to competitors such as Vietnam, Bangladesh, Sri Lanka and Pakistan. Many of India's garment factories must close or operate at half capacity to prevent new cases of Covid-19. According to the Economic Times, India T&G business in Tamil Nadu and Karnataka fear their orders will be halved within 2H21F as they cannot send samples to help global brands prepare new collections.

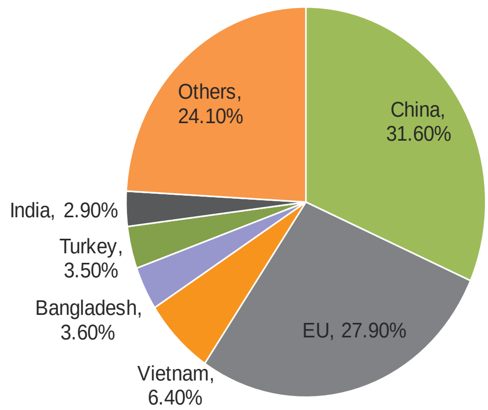
Myanmar 's textile & garment industry is dealing with twin headwinds: increasing infection cases and the political turmoil on Mar 21. In 1H21, employment in T&G companies decreased by an estimated 31% yoy due to factories closure.

Figure 11: India is the main competitor of Vietnam in the U.S. market (accounted for 10.94% the U.S. import turnover in 5M21)



Sources: OXTEA, VNDIRECT RESEARCH

Figure 12: Vietnam becomes the 2nd largest garment exporter in the world in 2020



Sources: WTO, VNDIRECT RESEARCH

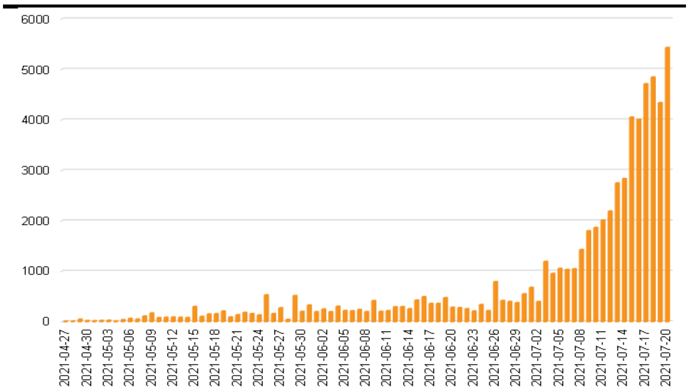
Although Vietnam is facing the 4th outbreak of Covid-19, we expect that the adverse effects of the political situation and the epidemic on Myanmar and India are opportunities for Vietnam to increase market share in the U.S. and Korea. We believe TNG, MSH and GIL are likely the key beneficiaries as their factories locate in Thai Nguyen, Nam Dinh, Hue, which are out of the current outbreak centre. The U.S. market is the main export market of GIL, accounted for 70% of GIL's export revenue in 1H21. Whereas TNG and MSH showed a significant earnings growth in 2Q21 partly thanks to FOB orders to be shifted from India and Myanmar to Vietnam. We believe that the increase in orders benefiting from the supply disruption in the Indian and Myanmar markets will contribute 20% and 15% to TNG and MSH's revenue, respectively in FY21F.

We see a few challenges to blur the recovery outlook in 2H21

2H21 earnings growth might be weakened due to the current wave.

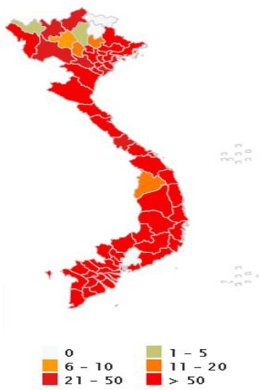
The COVID-19 outbreak in the South region could disrupt supply chains again as companies are unable to ship raw materials and lack the human resources to ensure timely deliveries. According to Vitas, the prolonged social distancing period will greatly affect the business results of T&G companies when 50% of factories are located in the South. Currently, the proportion of factories that have to close has reached 30-35%, mainly small and medium enterprises, due to insufficient funds to implement "3 on-site" for employees.

Figure 13: Daily new cases since the fourth outbreak of COVID-19 infections in Vietnam



Sources: WHO, VNDIRECT RESEARCH

Figure 14: Coronavirus spread across the country (total confirmed cases, per province)



Sources: WHO, VNDIRECT RESEARCH

According to Vietnam Textile and Apparel Association (VITAS), Vietnam T&G industry is facing challenges due to a shortage of workers and sluggish vaccination rate for the industry. When the Covid-19 is under control by the end of Aug-21, T&G export turnover in 2021 may only reach US$33bn (-6% yoy), fulfilling 84% of the Vietnam government's guidance for 2021 (US$39bn).

Rising transportation cost is a pain point of Vietnam T&G industry

Container freight costs increased three times in 1H21. We think that the shortage of empty containers and high logistics costs in 2H21 may affect businesses with ODM and Original Brand Manufacturing orders. Furthermore, VITAS forecasts that if the Covid-19 epidemic is under control by the end of Aug-21, the number of employees is expected to reach only 60-65%. Therefore, the shortage of human resources is challenging for Aug-21 and 3Q21.

Figure 15: Listed T&G manufacturers FY21 earnings outlook (Unit: in VNbn, otherwise noted)

Companies	NP in 1H21	NP's plan	VND's NP forecast	Comment
MSH	216	283	448	Likely to achieve our FY21F NP forecast thanks to 1) positve results in 1H21 ; 2) unaffected by the 4th Covid-19 as the factories locate in Nam Dinh which is out of the current outbreak centre and 3) Song Hong 10 factory expects to increase 20.0% capacity of MSH in 4Q21.
GIL	186	180	350	Be able to reach our FY21F NP expectation, driven by 1)solid earning growth in 1H21 and 2) the new cooperation with online retail giants such as Amazon and IKEA 3) unaffected by the 4th Covid-19 epidemic as the factories locate in Hue which is out of the current outbreak centre
TCM	120	290	323	Fall short of our expectation due to the shortage of gauze mask and anti-virus fabric orders in 2Q21 and 3Q21. Furthermore, TCM's factories located in Vinh Long province which is hardest hit by Covid-19 outbreak. Although TCM have implemented "3 on-site" for employees, the worker's arrangement to stay at factories will cause additional G&A expense in FY21F (15% G&A expense in FY21F).
STK	141	248	296	Likely to achieve our FY21F NP expectation, underpinned by 1) orders to be shifted from virgin yarn to recycled yarn and 2)gain more market share from the U.S. market thanks to the low preliminary anti-dumping duty. Moreover, we forecast that additional expenses for meals, accommodation and Covid-19 vaccination for employees will amount to VND3bn (1% our NP FY21F forecast) as lower worker volume of yarn manufacturers compared to garment businesses.
TNG	83	175	230	Likely to accomplish our FY21F forecast thanks to 1) the earning of industrial park segment in 2H21 is expected to reach VND70bn and 2) take advantage from shifting order from India and Myanmar in 2H21 and 3) uneffected by the 4th Covid-19 out break.

Sources: VNDIRECT RESEARCH, COMPANY REPORTS

STK is our sector pick

We like Century Synthetic Fiber Corp (STK VN, ADD, TP: VND50,600) for:

- The growing global demand for recycled yarn will be the key driver for STK' revenue growth over FY21-23F. In addition, the company adopts Spinning chips technology which easily switches between virgin and recycled yarns.
- The company can expand its capacity to 99,000 tons/year in FY23F and 123,000 tons/years in FY25F to capture the growing demand from both recycled and virgin yarn.

- We expect STK to expand its market share in the US market thanks to the low preliminary anti-dumping duty imposed by the US Department of Commerce on 26-May-21.
- STK earning is expected to grow robustly by 103.4% yoy in FY21F and 26.3% CAGR over FY21-23F.

Figure 16: Peer comparison

Company	Ticker	Recom.	TP VND	Mkt cap US$m	P/E(x) TTM	P/E(x) CY21F	3 year EPS growth CARG	P/BV(x) TTM	P/BV(x) CY21F	EV/EBITDA TTM	EV/EBITDA CY21F	ROE (%) TTM	ROE (%) CY21F
Vietnam National Textile & Garment Group	VGT VN	na	na	348	28.2	na	(4.3)	1.3	na	15	na	3.9	na
Thanh Cong Textile Garment JSC	TCM VN	na	na	244	22.0	18.1	13.81	3.4	3.5	13.9	10.8	15.4	14.1
Song Hong Garment JSC	MSH VN	HOLD	71,000	137	12.2	8.0	(14.0)	2.4	1.7	7.2	4.4	19.6	29.1
Century Synthetic Fiber Corp	STK VN	ADD	50,600	124	16.8	10.6	21.0	2.4	2.1	8.7	5.8	14.2	21.7
Viet Tien Garment Corp	VGG VN	na	na	79	18.5	9.8	(18.7)	1.1	1	4.2	na	7.1	9.8
TNG Investment & Trading JSC	TNG VN	na	na	73	11.2	na	17.61	1.4	1.1	na	na	13.0	na
NHA BE Garment Corp-JSC	MNB VN	na	na	22	12.5	na	5.11	1.8	na	8.2	3.6	11.5	na
Average					**17.3**	**11.6**	**2.9**	**2.0**	**1.9**	**9.5**	**6.2**	**12.1**	**18.7**
Median					**16.8**	**10.2**	**5.1**	**1.8**	**1.7**	**8.4**	**5.1**	**13.0**	**17.9**

Source: VNDIRECT RESEARCH, BLOOMBERG (Data as in 10 August 2021)

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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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