

Equity Research | HK & China | Textile OEM

17 October 2016

Growth intact led by market share gains

- We believe concerns over Nameson's (NS) growth outlook due to a weak US market are overdone, as strong order growth from Uniqlo and new client wins have more than offset such drop in 1H17.
- As of today, NS's order outlook for 2H17E from Uniqlo remains strong, led by market share gains. Although the US market fared better HoH, but YoY still points towards a decline.
- Besides, we expect GPM expansion of 0.4/0.8ppt YoY for FY17/18E, benefiting from RMB depreciation and cost synergies expected from its Vietnam plant. As of today, net D/E ratio is at a low single-digit, allowing debt headroom for potential M&As. We reiterate our BUY rating with the PT revised up to HKD2.0 (prev. HKD1.70), on earnings upgrade and rolling forward our PER basis to FY18E.

Strong order growth from Uniqlo. Uniqlo accounted for 58% of NS' total sales in FY16, as compared with its two other major clients, Tommy Hilfiger and Ann Taylor, which together accounted for 29%. In 1H17, the high double-digit percentage YoY sales order growth from Uniqlo has more than offset the double-digit percentage decline from its US clients. Moreover, the new client win with Gap Inc (GPS US) should help drive order growth as NS expects to receive c.1mn units of order (c.USD10mn) from Gap for FY17E. Thus, we are confident that NS will be able to achieve a 9% YoY revenue growth in FY17E.

Progress of Vietnam (VN) Phase II production plant expansion remains intact. Construction and equipment installation for VN Phase II is expected to be completed by the end of 2016, with official commencement of production in 2017. VN Phase I and II combined will add 17mn units of production capacity p.a., and thus on top of NS's existing production facilities in Huizhou, the PRC of 29.9mn units p.a. given the order commitment from Uniqlo, it will take up c.50% of the new capacity in VN. Besides, growing contributions from new clients, i.e. Gap and Adastria Group (2865 JP) are expected to be able to fill such new capacity. Further down the road, given the signing of EU-Vietnam FTA in Jan 2016, though finalised but not yet implemented, NS is expected to explore European customers.

Valuation. We adjusted our net profit estimates for FY17/18/19E by -1.0%/+2.2%/+7.2% respectively, after cutting our ASP assumption slightly for FY17E and adjusting upwards our GPM forecast for FY18/19E given the cost synergies from VN. We also roll forward our PER basis to FY18E, hence, our PT is adjusted upwards by 17.6% to HKD2.0 (prev. HKD1.70) based on 9.8x PER, still keeping a 10% discount to the average of its mid-stream peers. We reiterate our BUY rating, as medium-term growth is intact. NS currently trades at 7.4x PER for FY18E, undervalued compared to the average of 10.9x PER for the mid-stream plays.

Nameson Holdings (1982 HK)

Buy

(unchanged)

Price Target	HK\$2.0
(Revision)	(+17.6%)
(upside)	(32.5%)

EPS	2017E	2018E
revision	-1.0%	+2.2%

Close price	HKD1.51
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Market cap.	HKD3,133mn
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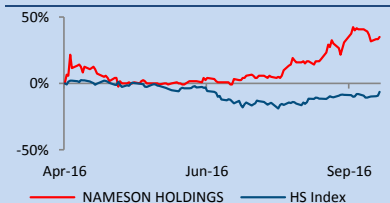
Free float	24.48%
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52-week range	HKD1.12 – 1.77
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3-mth ave. T/O	HKD5.3mn
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Price as of 13 October 2016

Stock rel HSI performance (%)



Analysts

SO Lai Shan, Jennifer
(CE No.: AHA295)
jenniferso@csci.hk +852 3465 5781

Major highlights

New client wins. NS used to be one of Gap's suppliers; attracted by the company's quality products and short lead time, Gap resumed orders with NS in 2016. NS expects to receive c.1mn units of order (c.USD10mn) from Gap for FY17E, which is equivalent to c.3% of our revenue estimates. Besides, the order volume from Adastria Goup is anticipated to increase materially in FY18E, given that the order size would normally pick up in the second year of business relationship. And further down the road, with the signing of EU-Vietnam FTA in Jan 2016, though finalised but not yet implemented, NS is expected to explore European customers.

GPM is on the rise. We believe NS will be able to grow its GPM slightly by 0.4ppt YoY to 22.5% in FY17E, given that RMB depreciation against the USD will help lower its COGS. According to the sensitivity analysis disclosed in its prospectus, a 5% drop in RMB will increase its net profit by HKD30-40mn. Besides, since NS's existing production plant was established in 2008 (subject to 10-15 yrs. of depreciation), its old plant has fully depreciated during the current period, which helps to offset the depreciation expenses arising from the new plants in VN. Hence, overall depreciation expenses should remain flat in FY17E. We expect greater GPM upside (+0.8% YoY to 23.3%) in FY18E, when production in VN phase II will be fully ramped up to c.13-14mn units. Meanwhile, direct labour and subcontracting charges usually account for 27% of sales in the PRC, where GPM is c.22%, and given that NS expects its VN plant can enjoy cost savings of c.10-13%, the GPM of the VN plant is expected to be over 30% if it is fully ramped up.

1H results usually accounts for c.60% of its full year. NS will be announcing its 1H17 results by the end of Nov. 1H results are important, due to the seasonality of its knitwear products, which usually account for c.60% of its full year results. Hence, it is indicative of its full-year performance. Management target a dividend payout ratio of c.35% for the full year.

Valuation

We have adjusted our net profit estimates for FY17/18/19E by -1.0%/+2.2%/+7.2% respectively, after cutting our ASP assumption slightly by 1% for FY17E and adjusting upwards our GPM forecast for FY18/19E by 0.3ppt./0.9ppt to 23.3%/24.0% given the cost synergies from VN.

We also roll forward our PER basis to FY18E, hence, our PT is adjusted upwards by 17.6% to HKD2.0 (prev. HKD1.70) based on 9.8x PER, still keeping a 10% discount to the average of its mid-stream peers. We reiterate our BUY rating, as medium-term growth is intact.

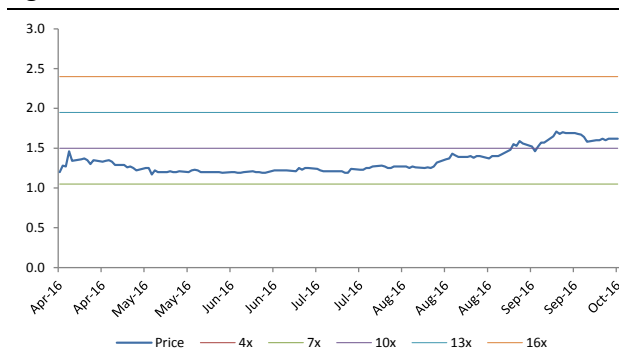
We estimate NS's core net profit 3-year CAGR to be 20.3%. NS currently trades at 7.4x PER for FY18E, undervalued compared to the average of 10.9x PER for the mid-stream plays.

Figure 1: Peers valuation

Name	Rating	PT	Ticker	Mkt Cap		Last Price	FYE	1-yr fwd	2-yr fwd	1-yr fwd	Sales	Op Profit	Cap Ex/	Dvd			EV/
				(bn HK\$)	Currency			PER	PER	PBR	growth	Margin	Sales	ROIC	ROA	Yield	EBITDA
HK listed																	
Upstream: yarn/ fabric																	
Texhong Textile	BUY	12.4	2678 HK	9.2	HKD	10.4	12/2015	8.2	7.4	1.7	1.0	11.8	10.5	14.5	6.9	2.9	6.1
Weiqiao Textile	NR	N/A	2698 HK	6.7	HKD	5.6	12/2015	4.9	3.7	0.3	(12.9)	18.3	3.8	4.7	3.5	5.3	1.5
Fountain Set	NR	N/A	420 HK	1.3	HKD	1.1	12/2015	N/A	N/A	N/A	(3.5)	2.4	1.9	N/A	2.6	N/A	N/A
Pacific Textiles	BUY	12.5	1382 HK	14.1	HKD	9.8	03/2016	14.7	13.5	4.3	0.3	16.7	5.1	22.9	20.2	8.2	10.2
Best Pacific	BUY	7.2	2111 HK	7.1	HKD	6.9	12/2015	17.5	15.1	3.6	10.1	19.9	6.0	13.5	12.0	1.9	11.7
Sub-Average				7.7				11.3	9.9	2.5	(1.0)	13.8	5.4	13.9	9.0	4.6	7.4
Up-mid stream: fabric & garment																	
Texwinca	HOLD	5.5	321 HK	7.3	HKD	5.3	03/2016	13.7	13.4	1.2	0.2	12.8	2.2	14.0	10.9	8.3	3.7
Shenzhou International	BUY	56.7	2313 HK	73.4	HKD	52.5	12/2015	21.2	16.9	4.3	13.5	22.6	16.1	16.0	14.7	1.5	16.0
Victory City	NR	N/A	539 HK	1.1	HKD	0.4	03/2016	N/A	N/A	N/A	(4.4)	8.3	15.7	3.7	2.3	13.0	5.1
Eclat	NR	N/A	1476 TT	23.7	TWD	88.0	12/2015	24.3	20.0	N/A	22.4	19.0	2.4	27.0	20.8	N/A	16.7
Sub-Average				26.4				19.7	16.8	2.8	8.0	15.7	9.1	15.2	12.2	7.6	10.4
Mid-stream: garment																	
Regina Miracle	NR	N/A	2199 HK	10.0	HKD	8.2	03/2016	19.9	13.8	3.2	21.2	12.6	17.9	15.9	11.5	0.7	13.1
Nameson	BUY	1.7	1982 HK	3.2	HKD	1.5	03/2016	9.7	7.4	2.0	7.7	10.3	7.0	13.1	11.0	-	8.4
Win Hanverky	NR	N/A	3322 HK	1.7	HKD	1.3	12/2015	6.5	6.5	0.7	7.5	7.0	5.9	9.7	6.9	8.9	2.6
Eagle Nice	NR	N/A	2368 HK	1.2	HKD	2.4	03/2016	9.1	8.1	1.0	1.2	10.9	1.6	10.2	8.0	10.0	5.1
Makalot	NR	N/A	1477 TT	7.3	TWD	35.3	12/2015	16.7	15.2	N/A	11.8	11.3	2.0	23.0	14.3	N/A	9.8
Sub-Average - (excl. Nameson)				5.0				13.0	10.9	1.7	10.4	10.5	6.9	14.7	10.2	6.5	7.6
Average of all - (excl. Nameson)				12.6				14.2	12.1	2.3	5.3	13.3	7.0	14.6	10.3	6.1	8.5

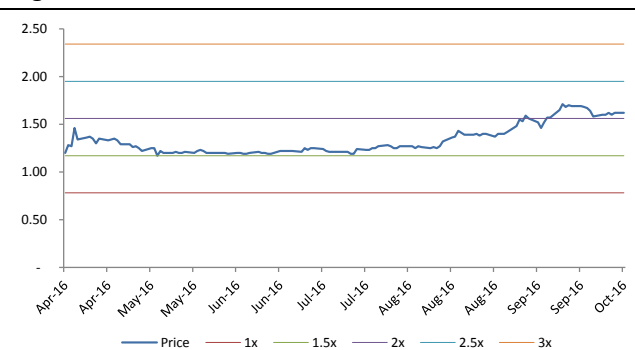
Source: CSCI Research, Bloomberg

Figure 2: PER band



Source: Bloomberg, CSI Research

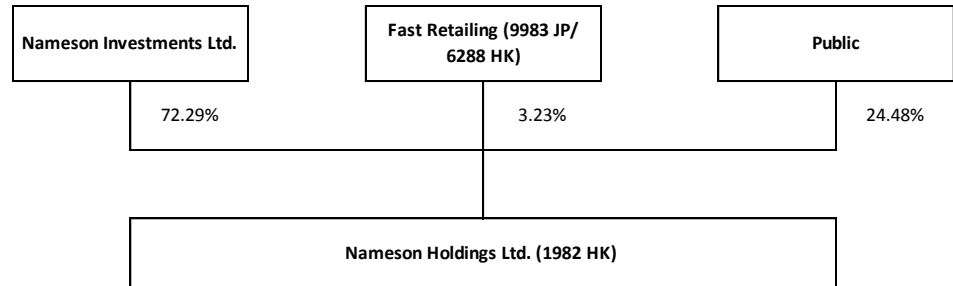
Figure 3: PBR band



Source: Bloomberg, CSCI Research

Company background

Figure 4: Shareholding structure chart



Source: Company, CSCI Research

Company overview: NS is the top-four knitwear manufacturer in the PRC, with a market share of 0.19% in 2014 based on revenue, according to the Euromonitor Report. The top five knitwear manufacturers in China captured a total market share of 2.03%. NS provides one-stop in-house solutions to its customers, who are international apparel brands, such as Uniqlo, Tommy Hilfiger and Ann Taylor. Their respective sales contributions were 58%, 21% and 8% in FY16. NS has long established business relationship with Uniqlo of over 20 years. NS is able to provide high quality cashmere yarn through its own on-site cashmere spinning machines. Orders are either directly placed by customers or through sourcing agent, based on a cost-plus pricing model.

NS's first production facilities (GFA: 350,315 sq.m.) was established in 2002 in Huizhou, Guangdong Province, with an annual designed production capacity of 29.9mn units of knitwear. In 1Q 2015, It opened its first production facility in Vietnam, on the outskirts of Ho Chi Minh City, with a GFA of 31,936 sq.m. for Phase one. It has started constructing Phase 2, with a GFA of 95,000 sq.m. Upon completion of construction in 2H 2016, NS's annual production capacity will rise to 46.9mn units of knitwear.

NS was listed in April 2016 on the Mainboard of the HK Stock Exchange at a new listing price of HKD1.20/shr, raising a net proceeds of HKD635mn.

Income statement (HKDm)

Year end: Mar	2015	2016	2017E	2018E	2019E
Revenue	2,568	2,766	2,993	3,589	3,817
COGS	(1,994)	(2,156)	(2,321)	(2,754)	(2,899)
Gross profit	573	610	672	834	918
Selling & distribution costs	(52.3)	(57.7)	(62.4)	(78.4)	(87.2)
General & administrative expenses	(235.2)	(267.8)	(257.4)	(308.6)	(328.3)
Other income	20.6	13.7	14.9	17.8	19.0
Other gains/(losses) - net	0.7	11.6	18.5	15.0	15.9
EBITDA	481	482	572	703	775
Depreciation & Amortization	174	172	186	223	237
EBIT	307	310	386	480	537
Net interest expenses/ (income)	20	26	6	(12)	(24)
Non-recurring items	27	(12)	0	0	0
JVs and associates	-	-	-	-	-
Pretax profit	314	271	380	493	562
Taxation	(41)	(40)	(55)	(72)	(82)
Minority interests	-	-	-	-	-
Net profit	273	232	325	421	480
Net profit (*adjusted)	252	275	324	421	480
Basic EPS (HKD)	0.18	0.15	0.16	0.20	0.23
Basic EPS (HKD) - (adjusted)	0.17	0.18	0.16	0.20	0.23
Diluted EPS (HKD)	0.18	0.15	0.16	0.20	0.23
Diluted EPS (HKD) - (adjusted)	0.17	0.18	0.16	0.20	0.23
DPS (HKD)	0.28	0.37	0.05	0.07	0.08

Balance sheet (HKDm)

Year end: Mar	2015	2016	2017E	2018E	2019E
Cash	334	222	599	718	1,186
Short term investments	154	140	-	-	-
Accounts receivables	39	43	47	56	60
Inventory	476	422	536	636	669
Other current assets	9	1	1	1	2
Total current assets	1,012	827	1,182	1,411	1,917
PP&E	924	893	1,057	933	776
Intangible Assets	-	-	-	-	-
Associates and JVs	-	-	-	-	-
Other long term assets	72	92	90	99	103
Total long term assets	996	985	1,147	1,033	879
TOTAL ASSETS	2,008	1,812	2,329	2,444	2,796
Short term debt	765	685	244	0	-
Accounts payables	141	128	152	180	190
Other current liabilities	214	170	204	260	291
Total current liabilities	1,120	983	600	441	480
Long term debt	143	171	171	171	171
Deferred tax	1	0	1	1	1
Convertible bonds	-	-	-	-	-
Other long term liabilities	-	-	-	-	-
Total long term liabilities	144	171	172	172	172
TOTAL LIABILITIES	1,264	1,155	771	612	652
Shareholders' funds	1,121	657	1,558	1,832	2,144
Minority Interests	-	-	-	-	-
TOTAL LIAB AND EQUITY	2,385	1,812	2,329	2,444	2,796
Net cash / (debt)	(574)	(634)	184	546	1,015

Source: Bloomberg, CSCI Research estimates

*Remarks: Adjusted net profit excludes listing expenses, gains/losses from PP&E disposals and derivative financial instruments. NS was listed in April 2016, it issued 575mn new shares at HKD1.2/shr.

Cash flow statement (HKDm)

Year end: Mar	2015	2016	2017E	2018E	2019E
EBIT	307	310	386	480	537
Depreciation & amortisation	(174)	(172)	(186)	(223)	(237)
Net interest expenses/ (income)	(20)	(26)	(6)	12	24
Taxes paid	(41)	(40)	(55)	(72)	(82)
Changes in working capital	84	(4)	(59)	(34)	(1)
Others	376	331	373	447	475
Cash flow from operations	532	400	452	610	716
Capex	(80)	(178)	(350)	(100)	(80)
Acquisitions	(122)	(540)	140	-	-
Disposals	-	-	-	-	-
Others	(23)	377	-	-	-
Cash flow from investing	(224)	(340)	(210)	(100)	(80)
Dividends	(427)	(120)	(114)	(147)	(168)
Issue of shares	-	-	690	-	-
Change in debt	182	(52)	(441)	(243)	(0)
Others	(36)	-	-	-	-
Cash flow from financing	(280)	(172)	135	(391)	(168)
Change in cash	28	(112)	377	119	468
Cash and cash equivalents at Beg. of the year	306	334	222	599	718
Cash and cash equivalents at End of the year	333	222	599	718	1,186
Free cash flow	488	261	107	497	612

Key ratios

Year end: Mar	2015	2016	2017E	2018E	2019E
Operating ratios					
Gross margin	22.3	22.1	22.5	23.3	24.0
EBIT margin (%)	12.0	11.2	12.9	13.4	14.1
EBITDA margin (%)	18.8	17.4	19.1	19.6	20.3
Effective tax rate (%)	12.9	14.6	14.6	14.6	14.6
Revenue growth (%)	10.6	7.7	8.2	19.9	6.4
Net income growth (%)	24.6	(15.2)	40.0	29.7	14.0
Net income (adjusted) growth (%)	(4.5)	9.3	17.9	29.7	14.0
Basic EPS growth adj (%)	(4.5)	9.3	(14.8)	29.7	14.0
DPS growth (%)	(0.2)	31.6	(85.4)	29.7	14.0
Efficiency ratios					
ROE (%)	22.4	41.9	20.8	23.0	22.4
ROCE (%)	34.6	37.4	22.3	24.0	23.2
Asset turnover (x)	1.3	1.5	1.3	1.5	1.4
Op cash / EBIT (x)	1.7	1.3	1.2	1.3	1.3
Depreciation / CAPEX (x)	(2.2)	(1.0)	(0.5)	(2.2)	(3.0)
Inventory turnover days	92.5	76.0	84.2	84.2	84.2
Accounts receivable days	6.1	5.4	5.7	5.7	5.7
Accounts payable days	24.9	22.9	23.9	23.9	23.9
Leverage ratios					
Net debt/ equity (%)	51.2	96.5	(11.8)	(29.8)	(47.3)
Net debt / EBITDA (x)	1.2	1.3	(0.3)	(0.8)	(1.3)
Interest cover (x)	15.2	11.8	65.5	(39.1)	(22.3)
Current ratio (x)	0.9	0.8	2.0	3.2	4.0
Valuation					
PER (x)	9.0	8.2	9.7	7.4	6.5
PER (x) - fully-diluted and adj. EPS	9.0	8.2	9.7	7.4	6.5
EV/EBITDA (x)	5.9	6.0	5.2	3.7	2.7
PBR (x)	2.0	3.4	2.0	1.7	1.5
Dividend yield (x)	-	-	3.6	4.7	5.4



Research

LIU Taisheng, Steven
TMT
(852) 3465 5652
stevenliu@csci.hk

SO Lai Shan, Jennifer
Consumer
(852) 3465 5781
jenniferso@csci.hk

CHAN Ka Yeung, Duncan
Commodity
(852) 3465 5654
duncanchan@csci.hk

TIAN Yang
Automotive
(852) 3465 5775
tianyong@csci.hk

SUN Lingxiao, Roger
Industrials
(852) 3465 5785
rogersun@csci.hk

XU Bo, Albert
Financials
(852) 3465 5789
albertxu@csci.hk

ZHU Kexin
Renewable energy
(852) 3465 5653
zhukexin@csci.hk

Institutional Sales & Trading

XIANG Xinrong, Ron
(852) 3465 5633
ronxiang@csci.hk

CAO Xiaogang, Glen
(852) 3465 5658
caoxiaogang@csci.hk

ZHANG Meng, Maurice
(852) 3465 5656
mauricezhang@csci.hk

HO Wen Hao, Jack
(852) 3465 5685
jackho@csci.hk

WANG Zhuo, Gary
(852) 3465 8655
wangzhuo@csci.hk

HO Hung Wei
(852) 3465 5687
hohungwei@csci.hk

LEE Ying Ju, Rose
(852) 3465 5707
roselee@csci.hk

LI Jiageng, Mike
(852) 3465 5636
mikeli@csci.hk

XIA Tian
(852) 3465 5670
xiatian@csci.hk

XU Xiaowei, Vincent
(852) 3465 5795
vincentxu@csci.hk

LI Tianyi, Miranda
(852) 3465 8653
mirandali@csci.hk

Company Rating Definition

The Benchmark: Hong Kong Hang Seng Index; Time Horizon: 12 months

Buy	12-month absolute total return: $\geq 10\%$
Hold	12-month absolute total return: $> -10\%$ but $< 10\%$
Sell	12-month absolute total return: $\leq -10\%$

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