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Retail Salesnote

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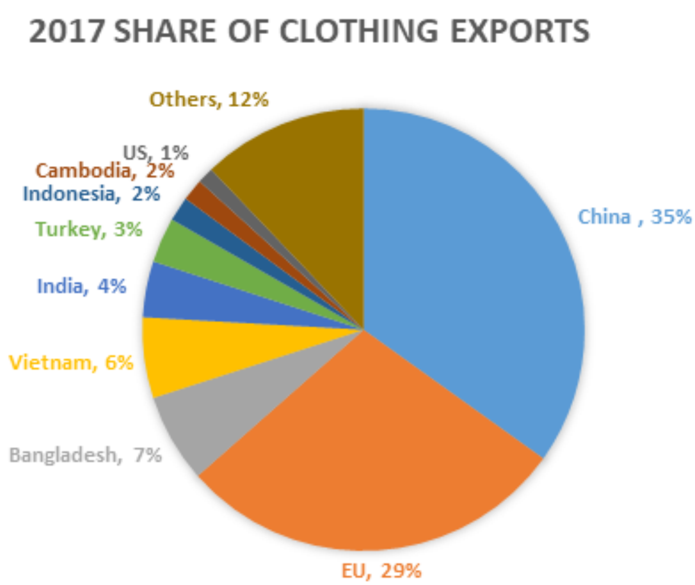
Textiles & Apparel sector poised for a sustained rebound.

The hills are ablaze with the sound of… humming textile factories [sorry Robert Wise]. News abounds of textile companies in Vietnam seeing a surge in new orders from both US and Chinese buyers, reportedly on trade war concerns. The odd fact is that textile and garments are yet to be included in the US tariff regime on Chinese imports. So it appears that the sheer threat of the next round of tariffs encompassing the textile sector has pushed US procurement managers to start diversifying their sourcing base. China + 1 is the new textile sourcing mantra.

China's interest in maintaining its textile and garment export leadership was anyways on the wane as wages rise, environmental concerns become paramount and as the government tries to reorient the economy towards consumption and high-end technology and innovation. The trade tensions have only accelerated what was a long-term, structural term.

Rather incredibly, even with textile factories relocating out of China for a few years now, China still dominates the sector with total textile and apparel exports amounting to USD257 bn in 2017 (EIU), of which around USD 39 billion went to the US market. The WTO estimates that China accounted for 36.2% of global textile exports and 34.5% of global clothing exports. Here are the market shares of the key Asian textile exporters:



Source: VNDirect Analysis, WTO

The combined clothing export market share of the top 5 Asian exporting nations, ex-China, is roughly just 57% of China's market share.

Though Vietnam is facing serious competition in the sector from the likes of Bangladesh and Cambodia, there is room for all to grow at China's expense. What is a ripple of capacity relocation out of China would be tantamount to a Tsunami for other textile and apparel exporters given how small their export share is versus the China's. Of course, India, by virtue of its sheer size would be expected to absorb the lion's share of what leaves China but issues with land acquisition and arcane labor laws mean that India's market share gains at China's expense are capped for now. Bangladesh, even with its large and cheap labor force, has its limitations due to poor infrastructure and a spate of recent revelations on poor labor conditions in the industry. Enter Vietnam.

Also worth noting is that 50% of Vietnam's ready-made garment exports are to the US, making it an outsized beneficiary of the US-China trade

We like **TCM** and **STK**. Both are expected to be outsized beneficiaries of this accelerated structural shift of the textile export base out of China. Both have seen a solid turnaround in their business and are trading at a 50-60% discount to the VN Index P/E, despite seeing 2-3x the pace of core earnings growth expected across the listed universe. TCM has rallied recently to almost touch our target price but is still an attractive bet for the longer-term. STK looks like a strong BUY at this juncture especially when you consider that the current US tariff regime already covers Chinese yarn, if not textiles and clothing yet.

		2018	**2019**	
Core EPS (VND/ share)	STK	2,503	3,487	
	TCM	3,574	4,207	
		2018	**2019**	
Core EPS growth (%)	STK	67%	40%	
	TCM	41%	18%	
		2018	**2019**	**TTM**
P/E (x) *	STK	7.6	5.4	5.7
	TCM	7.1	6.0	7.0
**P/E for 2018 and 2019 is based on core or recurring EPS*				

Has Oil bottomed-out for now?

There are better ways to bet on crude price swings than to buy into Vietnamese Oil & Gas equities. That being said, for those of a more speculative disposition and already trading in Vietnam, some pundits are predicting a rebound in crude prices after the secular decline seen in recent days. The logic is that, despite record production from Russia and rising production from Saudi Arabia, the re-imposition of sanctions on Iran has taken a lot of "slack" out of the market, even after accounting for the sanction wavers of 6 countries that are routine buyers of Iranian crude. Combine that with possible supply disruptions in Nigeria and Libya that could coincide with upcoming elections (historically observed to be the case) and the system-wide spare capacity looks rather thin. Note that Saudi Arabia has a spare capacity of around 1.5 to 2 million barrels per day, significantly lower than Iran's run-rate production of around 4.4 billion barrels per day, a large chunk of which will now be barred. Sure, the re-entry of shale could help add some slack but the pipeline capacity bottlenecks in the Permian basin mean that the increase in shale capacity will remain notional for some time yet.

Global demand conditions could be worsening so I take a measured view on oil into 2019 but a possible mini-rally before 2018 year-end cannot be ruled out, entirely. With Vietnamese oil & gas stocks having been battered down in recent days, a quick trade might be on the cards. I reiterate though that, given the multitude of geopolitical factors that are in the works, this trade is not for the faint-hearted.

Warmly,

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