

## China Textile Monthly Update

### Domestic cotton and cotton yarn prices continued to rebound

	Ticker	Rec	Mkt cap (HKD mb)	Ccy	Price	PT	Up/ dn (%)	PER 1-yr fwd	2-yr fwd	PBR 1-yr fwd	Dividend yield (%)	ROIC (%)
Texhong Textile	2678 HK	Buy	10.0	HKD	11.3	12.4	10.1	8.8	8.0	1.9	2.7	14.5
Weiqiao Textile	2698 HK	NR	6.5	HKD	5.4	N/A	N/A	4.8	3.6	0.3	5.4	4.7
Fountain Set	420 HK	NR	1.2	HKD	1.0	N/A	N/A	N/A	N/A	N/A	N/A	3.0
Pacific Textiles	1382 HK	Buy	14.6	HKD	10.1	12.5	23.5	14.5	14.2	4.7	7.9	22.9
Best Pacific	2111 HK	Buy	6.8	HKD	6.7	7.2	8.3	17.1	14.7	3.4	2.0	13.5
Tewinca	321 HK	Hold	7.6	HKD	5.5	5.5	(0.2)	13.7	13.4	1.2	8.0	14.0
Shenzhou International	2313 HK	Buy	71.5	HKD	51.1	56.7	11.0	22.1	17.7	4.2	1.6	16.0
Victory City	539 HK	NR	0.9	HKD	0.3	N/A	N/A	N/A	N/A	N/A	15.6	3.7
Regina Miracle	2199 HK	NR	11.8	HKD	9.6	N/A	N/A	19.5	14.8	3.7	0.6	15.9
Nameson	1982 HK	Buy	2.9	HKD	1.4	1.7	19.7	9.0	7.2	1.9	-	13.1
Win Hanverky	3322 HK	NR	1.7	HKD	1.3	N/A	N/A	6.5	6.5	0.7	8.8	10.3
Eagle Nice	2368 HK	NR	1.0	HKD	2.0	N/A	N/A	6.8	5.8	0.9	11.6	10.2

Source: Company, Bloomberg, CSCI Research estimates

- China extends the auction of state cotton reserves by one month through September, we expect total cotton ending inventory to decline to c.10.5mn tonnes in 2016, down from c.13mn tonnes in 2015.
- China's cotton yarn prices followed cotton prices to rebound in August, with 7.1% YoY growth, a reversal from the declining trend in 1H 2016. This is favourable to the average selling prices for textile OEMs given their cost-plus pricing approach, especially up-stream players, such as Pacific Textiles and Texhong Textile.
- On the contrary, prices on synthetic and polyester cotton yarns continued to be weak, primarily due to a weak oil prices.

#### Auction of state cotton reserves extends into September:

China has started auctioning its state cotton reserves for four months since 2 May this year. The auction was initially scheduled to run through the end of August, but it has been extended for another month until the end of September due to the lukewarm response and Chinese government's control on the issuance of additional quotas for cotton imports. As of 1 September, China has offered a total of c.2.4mn tonnes of cotton for auctioning in the market and c.2.1mn tonnes were sold, representing a purchase rate of 86.8%. Domestic cotton accounted for 85.6% of the total purchases while imported cotton accounted for 14.4%. These cotton reserves were sold at a price range of RMB9,730-16,490/tonne, or an average price of RMB13,185/tonne, a slight discount of 2.8% as compared to RMB13,562/tonne under the CC Index 328 during the same period. According to the China National Cotton Reserves Corporation, the total volume of cotton sold is expected to reach 2.5mn tonnes by the end of September. Hence, we expect the total ending reserves of China's state cotton will decrease to c.10.5mn tonnes on completion of the auction, compared with the level of c.13mn tonnes by the end of 2015.

#### Prices on cotton and cotton yarn continued to rebound in August:

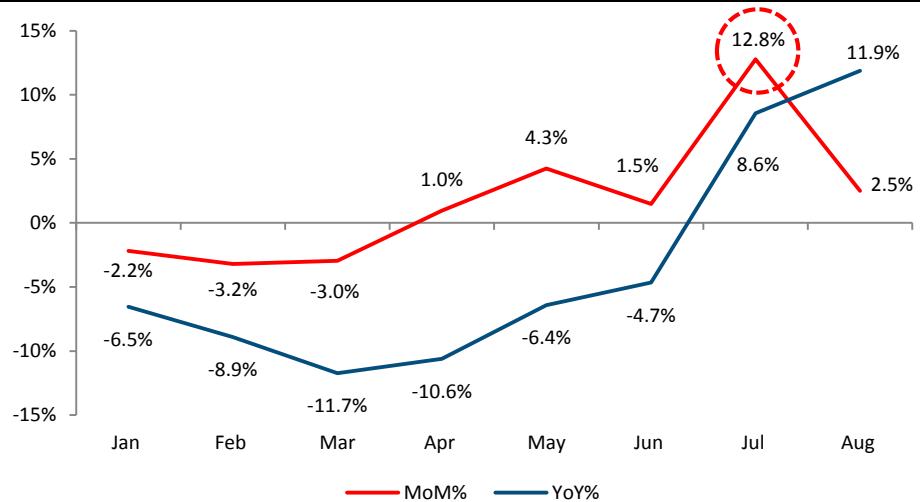
China's domestic cotton and cotton yarn prices continued to rebound in August. In the first eight months of 2016, the CC 328 Index has trended downward by 3.3% YoY, narrowing further from the 8.2% drop in 1H16, while the decline in the China cotton yarn index has also narrowed to only 3.8% from 6.2% in 1H16. Although the pace of rebound for cotton prices seems to have decelerated in August, as the CC 328 index has rebounded by merely 2.5% MoM in August, versus the 12.8% gain in July, we believe it was primarily attributable to the one month auction extension which has weighed on market prices due to an unexpected of c.400,000 tonnes of extra cotton inventory becoming available in the market. However, with falling production of cotton and consumption pretty much intact in China, this will lend support to domestic cotton prices.

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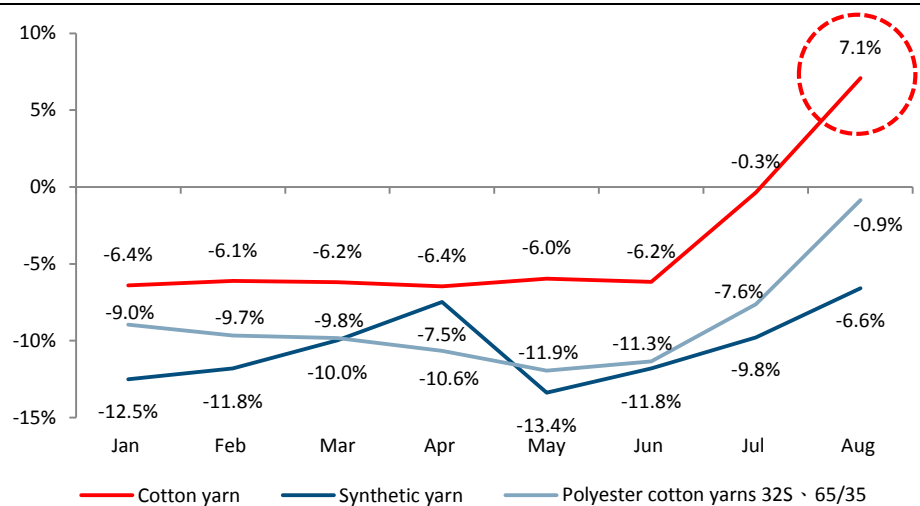
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**China's cotton yarn prices entered into a positive YoY growth territory in August:**

China's cotton yarn prices reversed from -0.3% YoY in July to gain 7.1% YoY in August (see Figure 2), one month after a major growth for China's cotton prices in July (see Figure 1). Nonetheless, for the first eight months of this year, the China cotton yarn index was still down 3.8% YoY, similar to the CC Index 328 which posted a 3.3% YoY drop over the same period. Meanwhile, however, synthetic and polyester cotton yarn prices have remained weak, posting 10.5% and 8.9% YoY decline in Jan-Aug this year, respectively (see Figure 3).

**Figure 1: China Cotton 328 Index (Jan – Aug 2016, MoM% YoY%)**


Source: Wind, CSCI Research

**Figure 2: China yarn prices – by categories (Jan – Aug 2016, YoY%)**


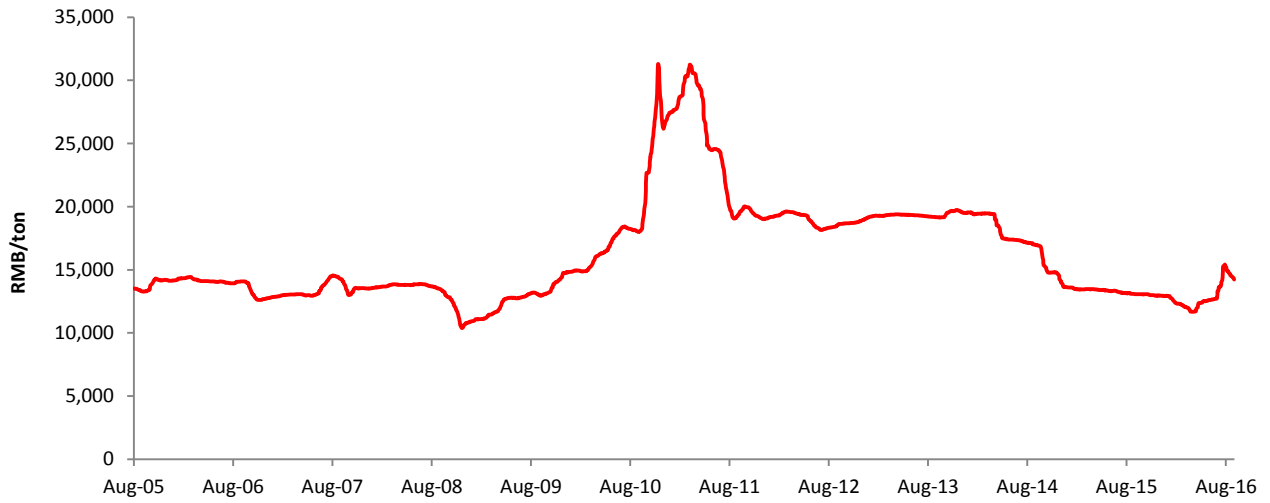
Source: Wind, CSCI Research

**Figure 3: Major cotton and yarn indices**

Major indices	YoY % Jan-Aug
CC328 Index (China domestic cotton)	-3.3%
CotLook A Index	6.2%
FC Index (Foreign import cotton)	-3.3%
China Cotton Yarn Index	-3.8%
China Synthetic Yarn Index	-10.5%
China Polyester Cotton Yarn (32S \ 65/35) Index	-8.9%

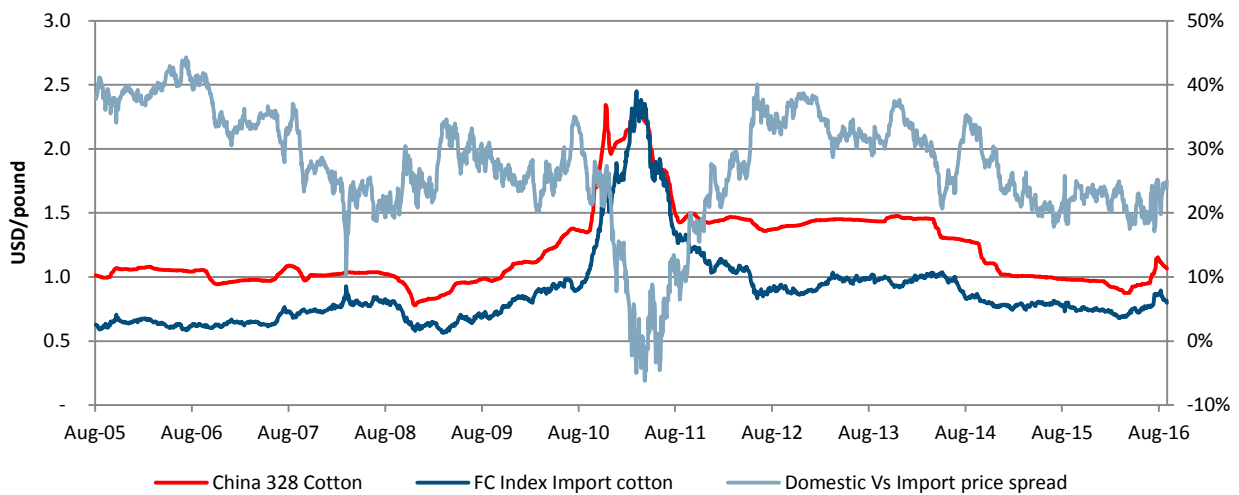
Source: Wind, CSCI Research

**Figure 4: China Cotton Price Index 328 (CC 328 Index) (Aug 2005- Aug 2016)**



Source: Wind, CSCI Research

**Figure 5: Cotton prices: domestic vs. import**



Source: Wind, CSCI Research



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

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

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