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HONG KONG RESEARCH
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Main Board Listing – Research

Pacific Textiles Holdings Limited [Stock Code: 1382] 互太紡織控股有限公司

Joint Global Coordinators, Joint Bookrunners, Joint Sponsors and Joint Lead Managers : Citigroup Global Markets Morgan Stanley

Co-Lead Manager : DBS Asia

Sector : Consumer Durables & Apparel
Business : Manufacture of knitted fabric and provision of dyeing, knitting, printing and finishing services

Total share offer: *358,234,000* shares
(25.00% of the enlarged share capital)

Public Offer: *35,824,000* shares (10%)

Placing: *322,410,000* shares (90%)

Greenshoe: *53,735,000* shares

Price: HK$4.15 – HK$5.50 per share

Market Cap: HK$5,947 million – HK$7,881 million

Pro-forma FY2006/07E P/E: 10.8x – 14.3x

Adjusted NTA per share: HK$1.84 – HK$2.17

Staffing: 6,721 (as of 25th April 2007)

Bookbuilding Period:
2nd May 2007 – 10th May 2007

Public Offer period:
7th May 2007 – 10th May 2007

Receiving banks: Hang Seng Bank,
ICBC (Asia),
Standard Chartered Bank (HK)

Share registrar: Computershare Hong Kong Investor Services Limited

Listing date: 18th May 2007

Business of Pacific Textiles

Pacific Textiles is a knitted fabric manufacturer set up in 1997. The Group is in the mid-stream of the textile supply chain, and offers fabric dyeing, knitting, printing and finishing services. It manufactures and supplies more than 3,000 designs and specifications of knitted fabrics to garment manufacturers worldwide.

Principal manufacturing facility of Pacific Textiles is located in Panyu, Guangdong Province with an aggregate floor space of approximately 294,400 m^2. For the 8 months ended 30th November 2006, the Panyu facility's production volume was 106.7 million pounds of weft-knitted (緯織) and warp-knitted (經織) fabrics.

Overseas wise, Pacific Textiles has a controlling stake in a "knitting and dyeing facility" in Avissawella, Sri Lanka, which is one of the largest intimate apparel suppliers in Sri Lanka and is the largest supplier to Victoria Secret. In addition, in 2005, Pacific Textiles, acquired a 33% interest in SPM Automotive Textile, a joint venture with Tokyo-listed companies Suminoe Textile and Marubeni Corporation, to manufacture car-seat fabrics and serve automotive customers with operations in southern China. In April 2006, the Group established a 50/50 joint venture Fillattice-Pacific with Fillattice S.p.A. to engage in the sales and marketing of specialty warp-knitted fabrics in the Asia-Pacific region. Both joint ventures remained loss-making for the 8 months ended 30th November 2006.

Major Shareholders after Listing *(Assuming the over-allotment option is not exercised)*

Mr. Ip Ping Im *(aged 70; a non-executive director, a co-founder and senior partner of the Group)*	27.91%
Mr. Choi Kin Chung *(aged 71; a non-executive director and a co-founder of the Group)*	11.94%
Mr. Wan Wai Loi *(an executive director, chairman and a founder of the Group)*, his spouse and children)	6.98%
Mr. Lam Wing Tak *(aged 56; an executive director and CEO of the Group)*	6.98%
Mr. Tsang Kang Po *(aged 57; an executive director, vice chairman and a founder of the Group)* and his spouse	6.98%
Dr. Lam King Man *(aged 51; an executive director of the Group)* and his spouse	2.09%
Mr. Lau Yiu Tong *(aged 59; a non-executive director of the Group)*	3.49%
Capital International Private Equity Fund IV, L.P. and CGPE IV, L.P.	8.63%
	75.00%

Use of Proceeds

Net proceeds from the offer are estimated to be HK$1,622 million *(Assuming the over-allotment option is not exercised, and at an issue price of HK$4.83 each, being the midpoint of the indicative price range)*

	HK$ million
For capital expenditure for the expansion and upgrade of the Group's facilities and operations	700
For repayment of existing syndicated loan and other bank loans	762
For general working capital	160

Financial Highlights

	Year ended 31st March			8 months ended 30th November
	2004 HK$ million	2005 HK$ million	2006 HK$ million	2006 HK$ million
Revenues	2,265.8	2,922.8	3,363.0	2,887.1
Gross profit	637.3	639.5	802.3	664.6
Operating profit	382.0	410.9	555.9	492.2
Attributable profit	**307.3**	**351.7**	**458.9**	**397.6**
Gross margin	28.1%	21.9%	23.9%	23.0%
Operating margin	16.9%	14.1%	16.5%	17.0%
Net margin	13.6%	12.0%	13.6%	13.8%

Sales by geographical locations (% of Total Revenues)

	Year ended 31st March			8 months ended 30th November
	2004 %	2005 %	2006 %	2006 %
Hong Kong	27.2%	21.8%	20.1%	21.7%
China	17.3%	25.5%	26.7%	24.6%
Sri Lanka	4.4%	5.0%	3.7%	3.3%
Vietnam	3.7%	1.7%	1.4%	0.4%
USA	3.2%	2.0%	1.2%	1.7%
Honduras	2.9%	4.5%	4.7%	4.5%
Macau	3.2%	2.0%	1.2%	1.7%
Jordan	2.9%	4.5%	4.7%	4.5%
Indonesia	2.5%	3.0%	4.0%	5.4%
Philippines	1.7%	1.7%	2.8%	3.1%
Others	24.9%	20.0%	15.8%	16.2%
Total	100.0%	100.0%	100.0%	100.0%

Strengths/Opportunities

- ✓ Entry barriers for fabric production are high as it is capital intensive and involves a greater demand for technology. The entry barriers are indeed rising given the tougher environmental requirements imposed on fabric manufacturers in the PRC.

- ✓ Pacific Textiles has been able to achieve higher-than-industry margins given its production scale and focus on the production of higher value-added, more complicated fabrics (i.e. warp-knitted fabrics) that command higher average selling prices.

- ✓ The Group has established strong indirect business relationships with a broad range of premium apparel brand owners such as Calvin Klein, Maidenform, Triumph, UNIQLO, VF Intimates and Victoria's Secret.

- ✓ The Group intends to pay out approximately 30% of its net profit as dividends for the year ended 31st March 2008.

- ✓ To be priced at 10.8x – 14.3x FY2006/07E P/E, valuation of Pacific Textiles is reasonable when compared with Hong Kong-listed sector peers - Fountain Set (stock code: 0420), Texwinca (stock code: 0321), Victory City (stock code: 0539) - given its higher margins. Fountain Set, Texwinca and Victory City are trading at FY2006/07E P/E ratios of 11.6x, 12.6x and 7.2x respectively.

Weaknesses/Threats

- × The Group's PRC operations are not directly impacted by the quotas imposed by the US and European Union on Chinese textiles and garments because its fabrics are largely sold to garment manufacturers outside these two regions. However, should similar restrictions be introduced by other countries on the Group's products, its business and operations could be adversely affected.

- × Yarn costs represent 66.2% and 68.2% of the Group's total cost of sales for the year ended 31st March 2006 and the 8 months ended 30th November 2006. Rising yarn prices will have adverse effect on the Group's production costs and hence its margins.

- × The Group receives a significant proportion of its revenue in USD and HKD, while a substantial majority of its operating expenses are denominated in RMB. Further RMB appreciation would have a negative impact on its margins.

Recommendation: Trading Buy

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