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HONG KONG RESEARCH**25th November 2004**

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Main Board Listing – Research

天虹紡織集團有限公司

Texhong Textile Group Limited [Stock Code: 2678]**Sponsor** : Goldbond Capital (Asia) Limited**Lead Manager & Bookrunner** : Goldbond Securities Limited**Sector** : Consumer Discretionary**Business** : Manufacture and sale of yarn and grey fabrics**Total share offer:** 218,000,000 shares
(25% of the enlarged share capital)**Public Offer:** 21,800,000 shares (10%)**Placing:** 196,200,000 shares (90%)**Greenshoe:** 32,700,000 shares**Price:** HK\$1.01 – HK\$1.38 per share**Market Cap.:** HK\$881 million – HK\$1,203 million**Prospective FY2004 P/E:** 7.2x – 9.8x**Staffing:** 5853**Book opens:** 23rd November 2004**Book closes:** 26th November 2004**HK Public Offer period:**30th November 2004 – 3rd December 2004**Share registrar:** Computershare Hong Kong
Investor Services**Receiving bank:** Standard Chartered Bank**Listing date:** 9th December 2004**Business of Texhong**

The Group is principally engaged in the manufacture and sale of yarn and grey fabrics and currently the 19th largest textile firms in China, according to China Textile Industry Association.

During the track record period, the Group's main focus was on the promotion and sale of its spandex stretch yarn and spandex stretch fabrics. Sales of spandex stretch yarn and spandex stretch fabrics in aggregate represented approximately 31.1%, 65.7%, 74.7% and 74.6% of the Group's turnover during the Track Record Period. Besides spandex stretch yarn and fabrics, the Group also manufactured over 390 types of yarn products and over 2,900 types of fabric products.

The Group currently has a textile manufacturing base comprising eight production plants, with a floor area of about 218,000 square meters in Jiangsu and Zhejiang Provinces and its customers are mainly PRC textile enterprises.

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

New Green Group Limited – wholly owned by Mr. Hong Tianzhu, Chairman and CEO	45.00%
Trade Partner Investments Limited*	18.75%
Wisdom Grace Investments Limited – Wholly owned by Mr. Zhu Yongxiang, COO	9.75%
Flourish City Investments Limited	1.50%
	<u>75.00%</u>

* The entire issued capital of which is beneficially owned as to 50.64% by Mr. Hong Tianzhu, 41.36% by Mr. Zhu Yongxiang, 2.24% by Mr. Sha Tao, 1.68% by each of Messrs. Tang Daoping, Gong Zhao and Hu Zhiping and 0.36% by each of Messrs. Yin Jianhua and Zhang Chuanmin.

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Use of Proceeds

Net proceeds from the offer are estimated to be HK\$193 million.

(Assuming the over-allotment option is not exercised and an issue price of HK\$1.20 per share, being the midpoint of the proposed range of HK\$1.01 and HK\$1.38)

	HK\$ million
Expansion of the Group's yarn production operations	169.8
Installation of a management information system	16.8
Acquisition of new equipment and the hiring of additional product development staff	2.0
General working capital of the Group	4.4

Financial Highlights

	Year ended 31 December			5 months ended 31 May
	2001	2002	2003	2004
	RMB'000	RMB'000	RMB'000	RMB'000
Turnover	343,883	730,152	1,034,340	497,516
Gross profit	62,505	139,702	155,896	71,856
Profit for the year/period	49,935	106,803	84,838	47,572

Strengths/Opportunities

- ✓ Abolition of the quota system on 1st January 2005 would simplify the process that the group deals with its existing overseas customers and opening up new markets.
- ✓ PRC domestic market provides ample growth opportunity to textile manufacturers as fibre consumption is still relatively low on a per capita basis, i.e. 6.4kg as compared with 38.1kg in United States. Spandex stretch textile products, that amount to over 70% of the Group's turnover, have gained wider usage in mainstream clothing in the past few years. This trend should help the Group's marketing efforts.
- ✓ The pricing of Texhong at 7.20x-9.80x FY2004 P/E is not demanding, compares with the sector P/E of 11x.

Weaknesses/Threats

- × The PRC textile manufacturing market is highly fragmented without any dominant player. Even the largest PRC textile manufacturer, Weiqiao textile (2698), finds it hard to gain pricing power over the buyers.
- × Prices of spandex stretch yarns and fabrics saw steady decline over the past few years as reduction of import tariff invited competition from abroad. Moreover, spandex has becoming "commoditized" after years of adaptation, thus driving the prices down. The Group thus depends on new product development to maintain its profit margin.

Recommendation: Trading Buy