

China Consumer (H/A)

Trade War 2.0? Our preliminary analysis

Industry Overview

Trade War 2.0? Too many ifs, more sentiment hit for now

The renewed market concern on Trade War 2.0 has triggered substantial debate and share price volatilities. In the near term, we see more impact on sentiment and flows, as 1) it could raise China's country risk premium and increase market volatilities, and 2) investors may examine the risk profile of the "going abroad" camp, which is normally regarded defensive amid domestic consumption weakness. On the fundamental side, we see limited ST impact as most companies have already reduced the US exposure or taken measures to mitigate geopolitical risk. The future impact is subject to too many ifs, but supply chain / business diversification should further accelerate. In this report, we identify names/sectors with US exposure under our coverage universe – white goods, textile OEMs, MNSO and WH.

White goods: The US no longer the largest export destination

The US is no longer the largest export destination for China white goods, after the US imposed 25% extra tariffs on China back in 2018, with Europe becoming the biggest customer of China white goods export. The US accounted for 11% of air-con, 17% of fridge and 5% of washing machine export volume in 2023, according to China IOL. For companies under our coverage universe, sales to the US generally represent high-single-digit% to low-teens% of total revenue, except for Haier which derived 30% of revenue from the US. Haier adopts OBM in the US using its acquired brand GE Appliance and uses local-for-local manufacturing strategy. We estimate direct exports from China to the US could be below 10% of total revenue for Haier. Other brands are also building up their non-China capacity to mitigate impact from US-China trade tension.

OEM: local-for-local, unless more tariffs levied on ASEAN

Our covered textile OEMs (including Shenzhou) now produce all the US orders outside China. The US was 16% of Shenzhou's revenue in 1H23. Any potential tariff hikes on China should not affect their US orders. Therefore, the impact for now is more on sentiment and valuation (especially given that Shenzhou is normally deemed as part of the "going abroad" camp). Meanwhile, some investors are concerned on tariffs extended to ASEAN, such as Vietnam. The past trade war has accelerated the supply chain shift out of China to ASEAN, with Vietnam as a key beneficiary. While Vietnam's COVID lockdown in 3Q21 has prompted brands to further diversify their supply chains out of Vietnam, Vietnam remains a sizable manufacturing hub for many OEMs. Shenzhou and major Taiwan OEMs derive high 20s to 50% of manufacturing capacities from Vietnam. While no evidence suggests more US tariffs will be levied on exports from Vietnam or other ASEAN countries in the foreseeable future, investors should not fully dismiss the worst-case scenario. As such, with supply chain diversification across countries (such as Indonesia) as an ongoing trend, OEMs are now expediting further diversification.

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Acronyms

MNSO: Miniso

OBM: original brand manufacturing

GMV: gross merchandising volume

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MNSO: limited impact from tariff hikes

MNSO's current US exposure is limited, should tariff hikes come through. 1) The US only contributed 4% of GMV, 5-6% of revenue and low single digit % of net profit to MNSO in 2023. 2) Currently, around 30% of US sales are locally sourced, including color cosmetics, toys and snacks, which are not subject to import tariffs. 3) MNSO also has diversified supply chains to some other ASEAN countries, which could offer some sourcing alternatives. 4) The US is a directly operated market for MNSO and MNSO has full control of retail pricing. In the event of extra tariffs, MNSO has the option to pass on cost pressure to consumers as it adopts a cost-plus pricing strategy.

WH: US-China pork trade largely negligible at present

The US accounted for 53% of revenue and 12% of EBIT in 9M23 (as WH owns Smithfield, the largest US pork company). WH's share price was hit during the 2018 US-China trade war, given the disruption to the US/China pork trade and negative impact on the US hog prices. Since then, the business has seen big changes, and we highlight the following facts. (1) **US-China pork trade:** the direct trade is very limited now, given already low pork price in China, 37% tariff on US pork and China's pork over-supply. (2) **US upstream:** the US hog production industry faces over-supply, partly due to weak exports. Investors generally believe trade wars could have further impact on exports and could prolong the recovery of hog prices (Smithfield has large exposure to upstream hog production). (3) **Potential US restructuring:** WH has publicly indicated its intention of a potential restructuring of Smithfield, without further elaborating on the timing and other details. Geopolitics might complicate business operations in the US, but some investors also expect it could potentially accelerate the future restructuring.

Stocks mentioned

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
HRSHF	6690 HK	Haier Smart Home	HK\$ 22.05	B-1-7
TTEF	600690 CH	Haier Smart Home	CNY 22.5	B-1-7
MNSO	MNSO US	MINISO	US\$ 17.66	C-1-8
XKTAF	9896 HK	MINISO	HK\$ 32.95	C-1-8
SZHIF	2313 HK	Shenzhen	HK\$ 67.95	B-1-7
WHGRF	288 HK	WH Group Limited	HK\$ 4.64	B-1-7

Source: BofA Global Research

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