

Indian Cotton Spinning Industry: Trends & Outlook

Nominal improvement in margins estimated for FY2024, despite an expected decline in revenues

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Indian cotton yarn exports likely to bounce back in FY2024 after a decline in previous year, owing to an expected increase in demand from Bangladesh and Vietnam.



- Domestic cotton prices had seen a lifetime high in H1 CY2022 but had declined steadily in H2 CY2022. For the 5M CY2023, the cotton prices had declined by ~20% compared to December 2022 prices, as the fresh produce hit the markets.



- Bangladesh has overtaken China to become the largest export market for Indian cotton yarn, accounting for ~38% share in FY2022. Bangladesh spinners were the beneficiaries following the ban on cotton from the Xinjiang region, and hence reliance on Indian cotton yarn exports has increased.



- Cotton yarn prices remained on a declining trend since June 2022 following the softening in cotton fibre prices and demand softening from the downstream apparel companies. ICRA expects the cotton yarn prices to remain steady in the near term and increase marginally in H2 FY2024 as demand from downstream companies is expected to pick up. The downstream apparel export companies are expecting a pickup in end demand for the spring summer 2024 season.



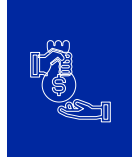
- Cotton production for CY2023 is projected to increase by 10% (estimates by office of textile commissioner) primarily due to higher acreage in Maharashtra and Gujarat.



- The gross spot margins for the spinners had reached a multi-year low in August 2022, on the back of high cotton fibre prices and reduced demand from downstream apparel companies. These had improved in H2 CY2022 and remained steady in 5M CY2023. ICRA expects cotton yarn gross contribution to contract marginally in FY2024. However, better factory utilisations will ultimately lead to higher EBITDA margins despite lower gross contribution margins.

Highlights on financial performance

Debt-funded capex to moderate in FY2024, and combined with an improvement in operating efficiency, ICRA expects the capitalisation and coverage metrics of the spinning entities to improve in FY2024.



- The average gross contribution margins for the spinners had declined sharply in FY2023 (24%) after a steep increase seen in FY2022 (+27%). The decline in FY2023 was led by high cotton fibre prices and demand remaining weak at the downstream companies. ICRA expects the gross contribution margin to contract marginally in FY2024, as expectation on marginal yarn price increase outpacing realization expectations.



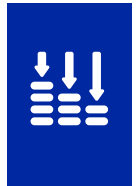
- ICRA expects domestic spinners to report a marginal volume growth from FY2024 onwards, primarily gaining through a shift in preference away from Chinese cotton and the expectations of demand improving for the apparel companies for spring/summer season in US and EU regions.



- ICRA expects the spinners to report revenue moderation in FY2024 (-7%), driven by an expected decline in realisations (FY2023 had high realisations in H1 FY2023) but partly offset by a moderate growth in volumes.



- Despite lower revenues, ICRA expects the operating margins to improve marginally in FY2024. The spinners are expected to benefit from the operating efficiencies arising from relatively higher volumes, and the expectation of logistics expenses reducing (as the bottlenecks at the ports worldwide experienced in 2022 are correcting).



- The industry had undertaken high debt-funded capex in FY2022, partly due to the deferment of major capital expenses in the Covid period (FY2020-21). Consequently, with a drop in demand in H2 FY2023, the coverage metrics of the industry had deteriorated in FY2023. Due to limited order visibility for FY2024, the spinners have halted any capex plans in the near term. ICRA expects a pick-up in capex announcements for FY2025, driven by modernization of machineries, and flow of demand on China plus one strategy.



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