

INDIAN APPAREL & FABRIC SECTOR

**Growth prospects remain
encouraging, even as near-term
challenges persist**

September 2023



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CAGR: Compounded Annual Growth Rate

CCEA: Cabinet Committee on Economic Affairs

CP TPP: Comprehensive and Progressive Agreement for Trans-Pacific Partnership; A free trade agreement between 11 nations including Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, and Vietnam.

CY: Calendar Year; refers to the twelve-month period starting from January 1 and ending December 31

EU: European Union (excluding United Kingdom, except where specifically mentioned)

EVFTA: EU-Vietnam Free Trade Agreement

FTA: Free Trade Agreement

FY: Financial Year; refers to the twelve-month period starting from April 1 and ending March 31

GSP: Generalised Scheme of Preferences; the scheme allows vulnerable developing countries to pay fewer or no duties on exports to certain countries extending such benefits.

GST: Goods and Services Tax

H1: First half of a year (Calendar or Financial)

H2: Second half of a year (Calendar or Financial)

MEIS: Merchandise Export Incentive Scheme

MMF: Man-made Fiber

PLI: Production Linked Incentive Scheme

Q1/Q2/Q3/Q4: Quarter of a Year (Calendar or Financial)

RoDTEP: Remission of Duties and Taxes on Exported Products

RoSL: Rebate of State Levies

RoSCTL: Rebate of State and Central Taxes and Levies

UAE: United Arab Emirates

UK: United Kingdom

US: United States of America

WTO: World Trade Organisation

YoY: Year on Year

USDA: The United States Department of Agriculture. Responsible for developing and executing federal laws related to farming, agriculture, forestry, and food.

13 listed companies considered comprises of Gokaldas Exports Ltd, S P Apparels Ltd, Celebrity Fashion Ltd, Pearl Global Industries Ltd, Arvind Ltd, Kewal Kiran Clothing Ltd, Loyal Textile Mills Ltd, Mafatlal Industries Ltd, Orbit Exports Ltd, Siyaram Silk Mills Ltd, Zodiac Clothing Company Ltd, Kitex Garments Ltd and Jindal Worldwide Ltd.

5 Unlisted companies considered comprises of Richaco Exports Private Limited (erstwhile Richa & Company), Richa Global Exports Private Limited, First Steps Babywear Private Limited, K. M. Knitwear Private Limited and Texport Industries Private Limited.

India placed favourably to grow at a faster pace than global apparel trade; likely to claw back lost share



EXHIBIT: Movement in global apparel trade (Past & Projected)

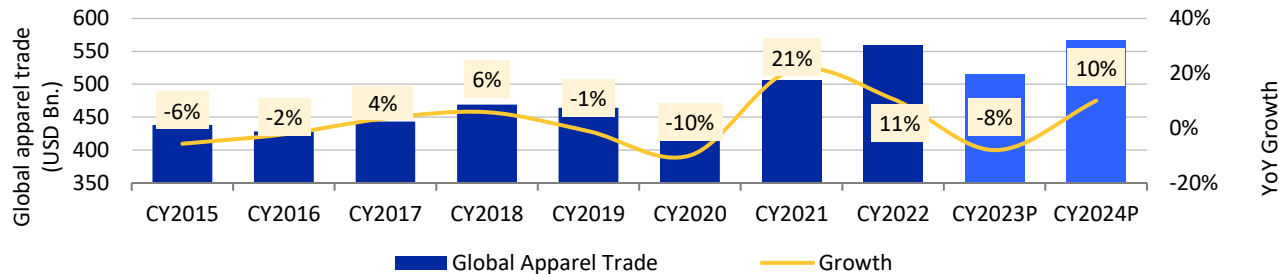
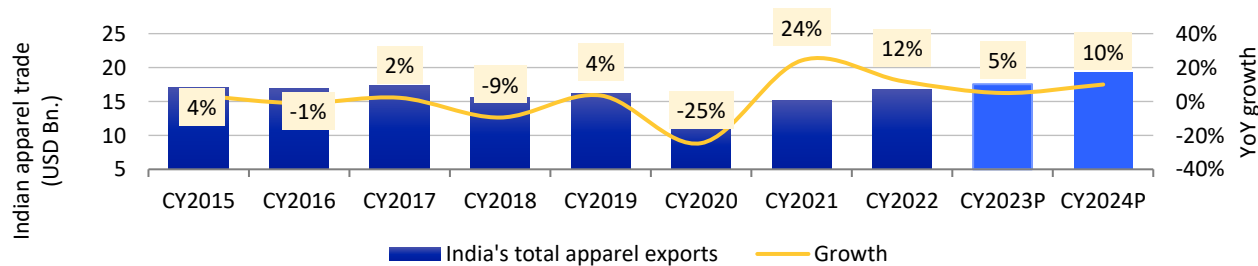


EXHIBIT: Movement in India's Apparel Exports (Past & Projected)



Source: UN Comtrade, Department of Commerce, CMIE, ICRA estimates

COMPETITION

Competitive pressures remain intense from countries such as Bangladesh, Vietnam and China



COST-SIDE PRESSURES

Sharp surge coupled with volatility in cotton yarn prices as well as increase in MMF prices in the past 2.5 years increased raw material costs for the companies.



DEMAND SLOWDOWN

Rate tightening and high inflation in key markets could be a potential threat to demand; retailers going cautious on inventory stocking



CHINA OPPORTUNITY

Restrictions on use of a major Chinese cotton variety, and China Plus One vendor strategy is expected to benefit Indian exporters over the medium to long term

FACILITATING ENVIRONMENT

Investments under PLI 1.0 scheme and PM MITRA Park could encourage capacity additions in the segment

EXPORT INCENTIVES

Extension of RoSCTL scheme for apparel exporters till March 2024 provides improved clarity, facilitating better pricing of products. Apparel Export Promotion Council (AEPC) has submitted a request to Govt of India in July 2023 towards extension of the scheme post March 2024. Clarity on the extension is still awaited. Given the importance, ICRA expects the scheme to be extended.



Investments in textile value chain under PLI scheme and PM MITRA Park and China Plus One strategy are expected to be the key growth drivers, even as apparel exporters step up efforts to withstand near-term challenges.

India's apparel exports had witnessed a decline in the last two quarters (ending Q1 FY2024), primarily due to inflationary pressures and a tepid economic environment in key markets

Apparel exports are expected to improve from H2 FY2024, on the back of expected demand recovery in US and EU regions.



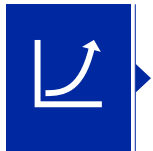
- The global apparel trade had increased by ~11% to USD 560 billion in CY2022. The imports by the EU and the US, which account for ~55% of the global apparel trade, however declined by ~9% YoY in 5M CY2023, following a ~18% increase in CY2022. The decline is attributable to the slowdown in demand amidst inflationary pressures and destocking by customers/retailers.
- Indian apparel exports declined by 17.8% to USD 3.7 billion in Q1 FY2024 on a YoY basis compared to a growth of 1% registered in FY2023. However, the depreciation of the rupee against the USD by ~8%, resulted in exports in INR increasing by ~8.8% in FY2023.
- The US and the EU (incl. UK) continued to be the largest export markets for Indian exporters, accounting for ~33% and ~32% share of the total exports, respectively, in FY2023.
- Indian apparel exports to the EU had increased by ~15% to reach USD 5.1 billion and those to the US rose by ~1.3% to reach USD 5.4 billion in FY2023 on a YoY basis. The overall share of the EU in Indian apparel exports improved to ~32% in FY2023 from ~28% in FY2022. India's exports to the UAE, however, witnessed a sharp 33% decline. The UAE acts as a re-exporting hub; difficult market conditions in its export markets had affected imports from India.
- Out of the approved 64 applicants the PLI 1.0 scheme in April 2022, 56 applicants completed the mandatory criteria for formation of a new company and approval letters have been issued to them. The Textile Ministry reopened the PLI scheme portal till October 31, 2023, for selecting participants for investing under the PLI scheme.
- PM MITRA parks will offer an opportunity to create an integrated textiles value chain and would encourage capacity additions in the segment. Seven sites in seven different states (Tamil Nadu, Telangana, Gujarat, Karnataka, Madhya Pradesh, Uttar Pradesh and Maharashtra) have been chosen for the PM MITRA Parks.

While higher raw material and higher employee expenses were exerting cost pressures, steps taken by companies to cut costs, renegotiated prices and INR depreciation protect their profit margins from falling significantly.

Large CAPEX investments for most players pushed back in FY2024, capex spending expected to pick up in FY2025.



- Despite the higher raw material costs and higher employee expenses, a steep fall in profitability was prevented in the past few quarters by renegotiation of prices with the customers. The OPBITDA margin of the sample set (of listed companies) was 8.3% in Q1 FY2024, and ICRA expects this to marginally improve ~9.0-9.5% in FY2024.



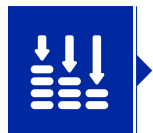
- ICRA expects its sample set to register a muted increase in total revenues (~3% increase to Rs. 27,255 crore) for FY2024, as apparel exports would continue to face headwinds till H1FY2024. ICRA expects a pick-up in volumes in H2 FY2024. This improvement would be on the back of liquidation of inventory at the importers' end with the onset of the Spring/Summer 2024 orders.



- A difficult operating environment had pushed back large CAPEX investments for most players, except, a brownfield expansion by one player. However, based on an expectation of demand revival from H2FY2024, industry players' strategies to take advantage of the China Plus One movement, and to capitalise on the PLI incentives (especially in the MMF value chain), ICRA expects a pick-up in CAPEX spending in FY2025.



- Despite the projected increase in debt-funded capital investments, the interest coverage ratio is expected to remain flat (at 5.7x in FY2024 and 5.5x in FY2025, against 5.6x in FY2023) and debt-to-equity ratio is likely to improve marginally (to 0.37x in FY2024 and 0.38x in FY2025, against 0.45x in FY2023).



- The trend of the number of upgrades exceeding the number of downgrades continued in FY2023, led by established apparel exporters who reported better-than-expected performance.



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