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INDIAN APPAREL & FABRIC SECTOR

Structural tailwinds to drive up industry prospects in FY2022 and FY2023

SEPTEMBER 2021

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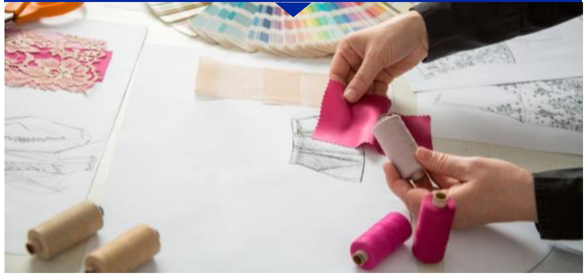

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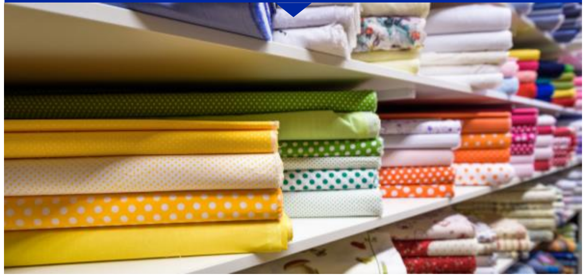

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Tailwinds set to outweigh headwinds for Indian apparel exporters

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COMPETITION

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

RAW MATERIAL PRICES

Sharp surge in cotton yarn prices in the current calendar year has increased raw material costs for the companies.

LOGISTICAL CHALLENGES

Global container shortage and high freight costs are causing supply side disruptions

DISCRETIONARY SPENDING

While overall discretionary spending had been affected by the pandemic, strong pick up is being seen across markets with Covid impact tapering off in key export markets

TRADE DEVELOPMENTS

Investments under PLI scheme, restrictions on use of a major Chinese cotton variety, and China Plus One vendor strategy to benefit Indian exporters

EXPORT INCENTIVES

Recent extension of RoSCTL scheme for three years for apparel exporters provides improved clarity, facilitating better pricing of products

Strong uptick in discretionary consumer spending, investments in MMF value chain under PLI scheme, clarity on export incentives and China Plus One strategy to be the key growth drivers, even as apparel exporters step up efforts to withstand near-term challenges

Highlights – Industry Trends

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Strong uptick in discretionary consumer spending, clarity on export incentives and China Plus One strategy to be the key growth drivers, as apparel exporters step up efforts to combat pressures arising from high raw material costs and logistical challenges.

- Compared to the first wave, India's apparel exports were much more resilient at the time of second wave.
- India's apparel exporters had built up a healthy order book prior to the second wave of the pandemic, supported by lifting of restrictions in the key markets of the EU and the US.
- Though risks of intermittent disruptions from incremental waves of infections, container shortages, delay in release of export incentives etc. remain, ICRA expects apparel exports to remain at near Pre-Covid levels going forward, with healthy recovery being seen in demand.
- Fibre mix of India's apparel exports contrasts with the global markets where MMF-garments account for the majority share. While India remains cotton dominated, the PLI scheme and the recent revision in GST structure which corrects inverted duty structure on MMF, are expected to encourage investments in MMF and help India garner a larger pie in that segment.
- Following several alternating stances on the export incentive structure and rates in the recent years, extension of RoSCTL scheme for three years provides improved clarity, facilitating better pricing of products, which had been a key cause for worry for exporters.
- In H1 CY2021, the US and the EU together reported a healthy recovery of ~22% YoY. While despite recovery, apparel imports remained lower than the pre-pandemic level, these stood at ~96% of the H1 CY2019 level and are expected to touch pre-Covid levels in H2 CY2021.

Highlights – Financial Performance & Credit Profiles

Financial performance and debt metrics of apparel exporters in FY2022 likely to be better than last year, despite intermittent disruptions

Improved scale, together with range-bound margins and reduced debt to translate into improved debt metrics in the near term; debt metrics for the sample projected to remain comfortable despite debt-funded capital expenditure likely under the PLI scheme in FY2023 and FY2024

- ICRA expects its sample of apparel exporters to report a healthy double-digit YoY growth in revenues in Q2 FY2022, reverting closer to the pre-Covid levels. While the order book positions remained robust, the second wave caused operational disruptions, resulting in revenues for ICRA's sample being ~10% lower than pre-Covid levels in Q1 FY2022, despite ~56% YoY growth.
- ICRA expects its sample of apparel exporters to report a healthy double-digit growth in revenues in FY2022, closer to pre-Covid levels, following a 16% decline reported in FY2021.
- While higher raw material prices are exerting cost pressures, steps taken by companies to cut costs, higher export incentives booked in the current fiscal (pertaining to Q4 FY2021) and scale benefits are expected to protect the profit margins.
- Limited capex in recent years, together with opportunities available in global market owing to China plus One vendor strategy, and increased attractiveness of investments in MMF value chain given the recently launched PLI scheme and changes made in the GST structure, are likely to encourage capital investments in the sector, by larger and mid-sized players.
- ICRA expects capitalisation and coverage metrics to remain comfortable, despite the projected increase in debt-funded capital investments, with healthy accrual generation and limited debt repayment obligations,
- Driven by multiple reasons, ICRA's credit ratio (ratio of upgrades to downgrades) for the apparels segment remained at less than 1x in the past five years. ICRA expects the credit ratio to stay higher than 1x in the current fiscal, led by recovery in performance of players.

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Thank You!