

INTRODUCING

CFO Journal.

FROM THE WALL STREET JOURNAL

GRAB THE LEAD

MarketWatch

Emerging Markets Report

July 11, 2011, 2:39 p.m. EDT

India's textile-firm stock rally might end

By Nick Godt, MarketWatch

MUMBAI (MarketWatch) — A slide in global market prices for cotton since April has led the shares of India's textile companies to rally strongly over the past several months. But these firms' pricing power, the cotton inventories they carry and the progress of monsoon rains will determine how the market reacts to their earnings, analysts say.

With cotton prices slumping since April, after their yearlong surge to reach 140-year highs in March, the shares of India's largest textile manufacturers have jumped from 20% to 50%.

Underlying the rally was the assumption that textile firms have already raised the prices on their products — be they for their own brands of jeans and cotton shirts, or the international brands they are licensed to manufacture.

"The cost pressure that this industry was facing has been tremendous and the margin pressure has been tremendous," said Sonal Varma, economist for India at Nomura. "But some of the cost has been passed on to consumers."

Arvind Mills Ltd. (BOM:IN:500101), one of the largest players, saw its shares rally 54% from their March lows. The firm provides fabrics as well as manufactured goods such as its own New Port University clothing, as well as licensed international brands such as Gant, Lee, Wrangler and Tommy Hilfiger.

China's exports, Malaysian protests

China's latest economic data shows exports rose to a record high and inflation surged to a three-year high, while in Malaysia demonstrators take to the streets of Kuala Lumpur demanding changes to the electoral system.

Shares of other major textile firms, Alok Industries Ltd. (BOM:IN:521070) and Raymond Ltd. (BOM:IN:500330), have rallied 23% and 52% respectively from their March nadirs. Other large textile manufacturers include Bombay Dyeing and Manufacturing Co. Ltd. (BOM:IN:500020), Century Textiles & Industries Ltd. (BOM:IN:500040) and Lakshmi Mills Co. Ltd. (BOM:IN:502958)

While the firms' share rally from the March lows has only partially compensated the slide since last year, how the market reacts when the companies post quarterly results over the next several weeks will depend on the outlook for global cotton prices and the progress of the monsoon in India.

Weather authorities have indicated weak rains in key producing states, especially in Gujarat, so far in July — which could lead farmers to reduce cotton production.

In India, where a majority of the population lives on less than \$2 a day, the government wants to ensure food-consumption needs are met and therefore subsidizes the production of certain food crops. When cotton production is increased to meet rising demand, it competes with these crops.



Reuters

An employee works inside a cotton factory at Mauayama, about 25 miles from the northern Indian city of Allahabad.

“Barring a weather calamity, I don’t see cotton prices surging again this year,” said Sageraj Bariya, managing partner at Mumbai-based commodities brokerage Equitorials. Nevertheless, he expects textile manufacturers’ earnings to remain impacted over the next few quarters as they work through bloated inventories.

Up until March, the slide in some textile stocks was even steeper than their recent rally, with Raymond Industries having slumped 41% from its 2010 highs, Alok Industries slumping 36% and Arvind losing 27%.

Cotton prices had surged to \$2.197 a pound in early March, a 140-year high, as freezing temperatures in China, along with flooding in Pakistan and Australia cramped production.

Since then, cotton futures for December delivery (NYSE:CT1Z) have plunged nearly 50% to reach a seven-month low of \$1.12 on Friday on ICE in New York.

The latest part of the surge early this year was believed to have been fueled by speculation, as traders, who buy cotton from farmers, held onto inventories in hope of selling at higher prices. Textile manufacturers themselves had loaded up on cotton in case prices did continue to surge.

“Most of the [textile] companies’ results are not going to be that great at all because they carried inventories and have bought so much in bulk,” said Bariya at Equitorials.



Alok Ltd.

Although data on company pricing are scarce, inflation in textiles prices in India was 15.9% in May from the year earlier, contributing to the surprise 9.1% year-on-year jump in wholesale inflation that month, according to government data. June inflation numbers will be released Tuesday.

The Indian government imposed export restrictions last year to contain the impact of surging prices on both the domestic textile industry and on consumers. India is the world’s second largest producer and exporter of cotton, behind the United States, and the second largest consumer of cotton behind China.

Cotton heritage

The Indian subcontinent has a long history with cotton. More than 4,000 years ago, during the heydays of the Indus civilization in modern-day Afghanistan, Pakistan and northern India, cotton was cultivated, textiles manufactured and sold to eventually be worn as garments as far away as Rome.

Of course, Mohandas Ghandi and India’s independence movement used a spinning wheel, now found at the center of the Indian flag, along with a boycott of British cotton to restore the country’s control over its domestic production and bring about the end of the British Raj.

Since the 1990s, though, globalization has brought about its own hardships on India’s cotton industry, mostly on farmers. Tens of thousands of farmer suicides have been reported over the years, as wide fluctuations in prices and indebtedness led many to despair.

Heavy subsidies from the United States, the world’s largest exporter of cotton, and from Europe, had often resulted in keeping prices low.

In more recent years, the rise of domestic demand from both China and India, along with escalating climate-change disasters in producing countries, has led many commodities, including cotton, to surge.

The government is trying to balance India’s own enormous needs while building up its textile industry to both provide for, and compete, with China’s.

Through the state-run Cotton Corp. of India, the government controls the trade and the export of the commodity,

and also subsidizes higher production to keep domestic prices low enough for the industry.

Export restrictions, which were put in place since April of last year, were recently relaxed as domestic production was boosted and following the recent slump in cotton prices.

Following a spate of farmer suicides in 2007, the government has put in place measures to provide a minimum price to farmers. That also means growers didn't reap the benefit of the recent surge in prices, according to Madan Sabnavis, chief economist with Care Ratings.

"The farmer doesn't receive the market prices, but the intermediaries such as the traders and the export companies do," he said. "Still, we haven't seen [suicides] happening this year, and the policy of providing a minimum price has helped."

Copyright © 2011 MarketWatch, Inc. All rights reserved.
By using this site, you agree to the [Terms of Service](#) and [Privacy Policy](#).

Intraday Data provided by SIX Telekurs and subject to terms of use. Historical and current end-of-day data provided by SIX Telekurs. Intraday data delayed per exchange requirements. Dow Jones Indexes (SM) from Dow Jones & Company, Inc. All quotes are in local exchange time. Real time last sale data provided by NASDAQ. More information on NASDAQ traded symbols and their current financial status. Intraday data delayed 15 minutes for Nasdaq, and 20 minutes for other exchanges. Dow Jones IndexesSM from Dow Jones & Company, Inc. SEHK intraday data is provided by SIX Telekurs and is at least 60-minutes delayed. All quotes are in local exchange time.