

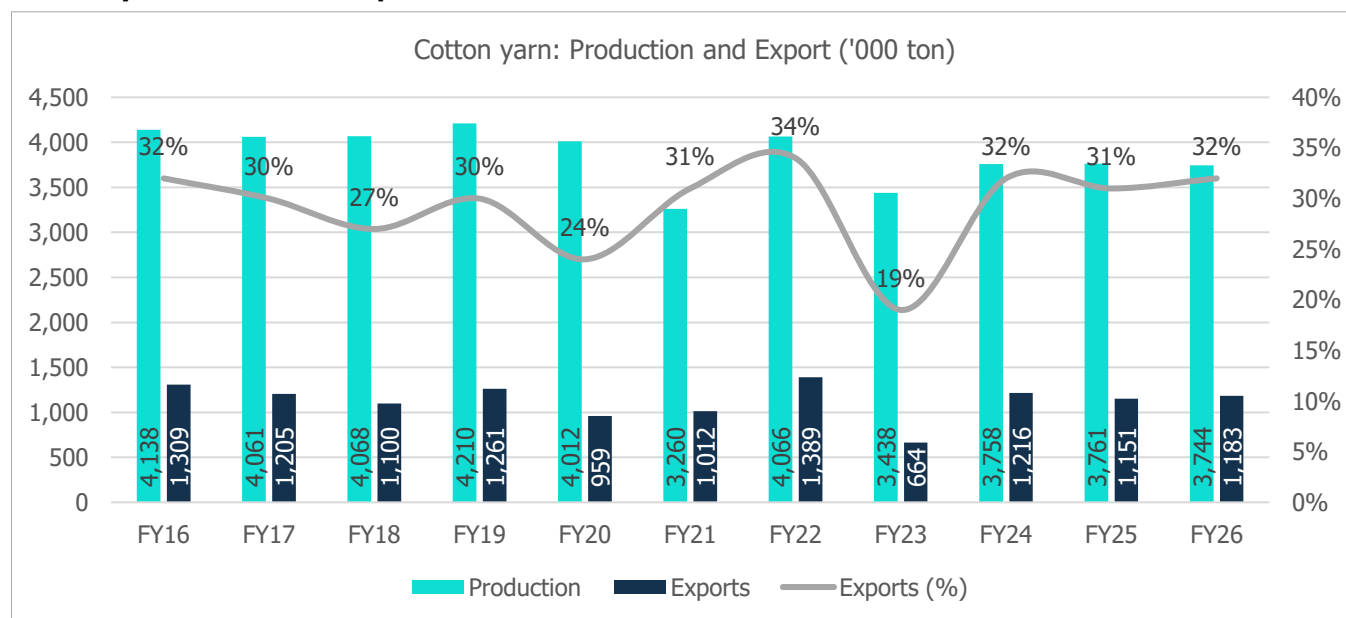
Cotton Yarn Industry to Spin 150-200 bps Margin Improvement in FY27

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Synopsis

- The Indian cotton yarn industry experienced a notable recovery in Q4FY26 after nearly three years of subdued performance. The improvement was supported by easing U.S. tariff-related uncertainties, improved order flows from apparel and home textile exporters, resurgence of Chinese demand, and improving sentiment around India–UK and India–EU free trade agreements.
- A key structural change for the industry has been supply-side rationalisation. Nearly 10-12 million spindles have been phased out over the past few years, reducing effective capacity to about 40-44 million spindles. This has improved the demand–supply balance for organised players and created a more sustainable pricing environment.
- Concurrently, Indian cotton has regained its global competitiveness as domestic cotton prices have moved closer to international price levels. Consequently, cotton yarn spreads have recovered significantly from around Rs 95-100/kg in FY26 to ~ Rs 120–125/kg currently, supported by better demand, tighter supply, and cotton price parity.
- The favourable demand-supply dynamics and pricing environment are expected to continue in FY27, leading to an envisaged improvement in the operating profitability margin of the Indian cotton yarn industry by 150-200 basis points in FY27 compared with FY26. However, the sustainability of the same beyond FY27 will depend on trends in Chinese demand, cotton price movements, geopolitical developments, and the pace of recovery in the global downstream consumption.

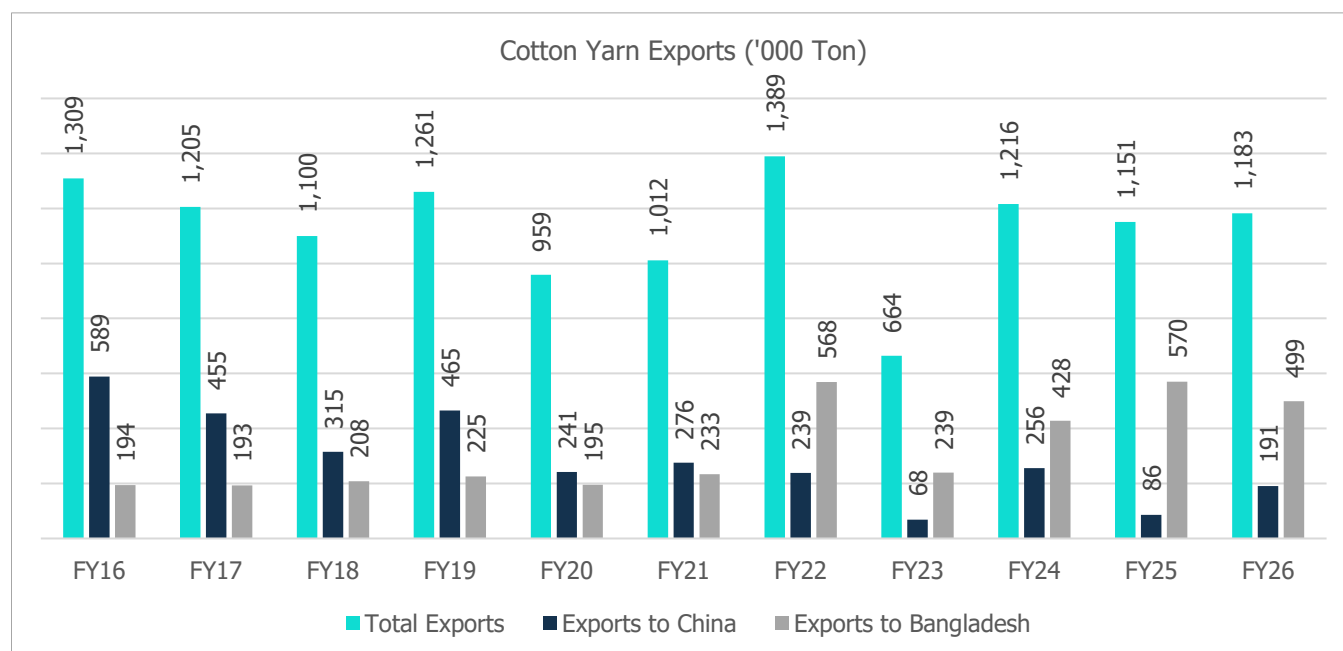
Recovery in Cotton Yarn Exports



Source: CMIE; Compiled by CareEdge Ratings

India's cotton yarn exports remain an important demand lever for the industry, historically accounting for around 25-35% of domestic cotton yarn production. The demand for cotton yarn in FY22 was strong, driven by downstream demand for home-textile products and the advantage of lower domestic cotton prices compared to international prices. However, in FY23, Indian cotton yarn exports faced challenges due to the disparity between domestic and

international cotton prices, affecting India's global competitiveness. Consequently, cotton yarn exports stood at 19% of cotton yarn produced in FY23. The global demand slowdown, driven by high inflation and recessionary pressures in developed economies such as the USA and the European Union, further impacted exports.



Source: CMIE; Compiled by CareEdge Ratings

Indian cotton yarn exports increased by 3% in FY26 to 11.83 lakh tonnes, reversing the decline seen in FY25. The improvement was more visible in Q4FY26, when exports grew 11% YoY to 3.38 lakh tonnes, indicating a stronger finish to the year. China emerged as the key growth driver, with exports to China surging 121% in FY26 and 339% YoY in Q4FY26, reflecting renewed demand for Indian cotton yarn from Chinese textile manufacturers. The increased Chinese demand is attributed to reduced cotton acreage, lower domestic cotton production, improved domestic textile demand in China, and the economic advantage of importing yarn rather than cotton.

Domestic Cotton Yarn Capacity Reduction Restores Demand-Supply Balance

The most important structural development in the industry over the last few years has been the curtailment of spinning capacity. It has been observed that ~10-12 million spindles (~20% of installed capacity) in the industry have been phased out over the last few years, mainly due to cyclical pain and structural weakness. A prolonged period of low cotton yarn spreads, combined with demand disrupted by tariffs and geopolitics, severely squeezed profitability, leading to underutilization. Many smaller mills faced financial stress, working capital shortages, and rising electricity costs, rendering operations unviable. Older plants with obsolete machinery could not compete with modernised units on efficiency, power consumption, or quality.

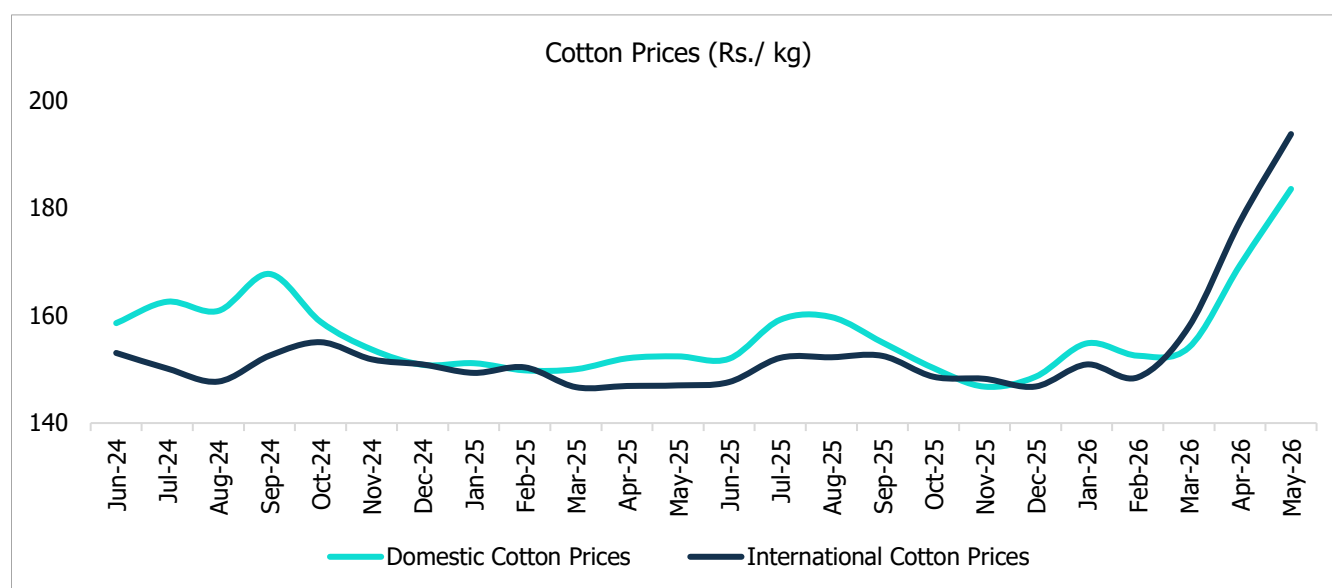
Importantly, the capacity exits have been largely concentrated among smaller spinning units with fewer than 30,000 spindles, characterised by older machinery, limited scale, and weaker working capital support. Such capacities are unlikely to be revived in any meaningful manner even if yarn spreads remain favourable, indicating that the recent supply rationalisation is structural rather than cyclical. Further, the increased capital cost per-spindle has reduced the economic viability of establishing new cotton spinning facilities with capacities of up to 50,000 spindles. Even large-scale greenfield projects would typically require 12-18 months to become operational and contribute meaningfully to domestic supply. Consequently, the ongoing industry consolidation has strengthened the demand–

supply balance for organised cotton yarn players, supporting a more sustainable pricing environment and improved profitability prospects.

Cotton Yarn Spread Recovery Supported by Demand and Restoration of Cotton Price Parity

Demand for cotton yarn has strengthened across both domestic and export markets, supported by the resolution of U.S. tariff-related uncertainties, improved order flows from apparel and home textile exporters, and growing optimism around the India-UK and India-EU Free Trade Agreements. Export demand across the value chain from key markets such as the U.S., Europe and Bangladesh has improved, while domestic demand has also remained healthy. An increase in export demand from China also supported the overall demand for Indian cotton yarn in FY26.

The parity with international cotton prices enhances the competitiveness of Indian cotton yarn players. In FY23 and for much of the subsequent period, Indian cotton remained at a premium to international cotton, reducing the competitiveness of Indian yarn exports and compressing cotton yarn spread and margins. Domestic cotton prices have now broadly aligned with international prices, restoring India's competitiveness in global markets and leading to a recovery in the cotton yarn spread.



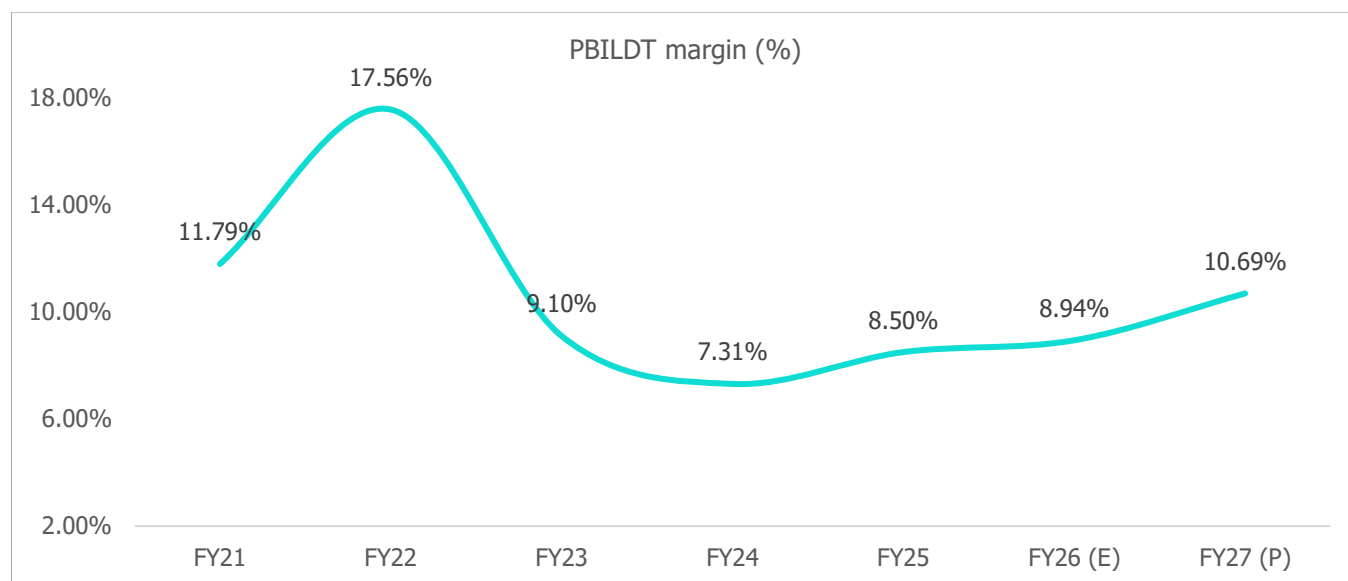
Source: CMIE; Compiled by CareEdge Ratings

Healthy export demand from China, steady domestic offtake, lower procurement cost for cotton inventory bought earlier in the season and tight supply dynamics translated into an improvement in cotton yarn spreads from Q4FY26 onwards. Historical spreads, which had risen to over Rs 150/kg in FY22, moderated to about Rs 95-105/kg in the subsequent period. Average spreads have improved from ~Rs 95-100/kg in FY26 to around Rs 120–125/kg since April 2026.

CareEdge Ratings expects a favourable spread environment to continue in FY27, supported by healthy export demand and the expectation of continuation of parity in cotton prices due to the removal of import duty on cotton till October 31, 2026.

Profitability Outlook for FY27

Improved spreads and stronger operating leverage are expected to boost the operating profitability of Indian cotton yarn spinning companies in FY27. Consequently, the Indian spinning industry is expected to register a Y-o-Y revenue growth of around 10% in FY27, driven by 3-4% volume growth and the balance through higher sales realisation, while the operating margin is expected to expand by 150-200 bps over FY26. Despite a better cotton yarn spread, improvement in the PBILDT margin will be constrained by a gradual increase in conversion costs and overheads driven by inflationary pressures.



Source: Ace Equity; Compiled by CareEdge Ratings

Note: The above study represents cotton yarn spinners accounting for ~30% of the industry.

Chinese demand has historically remained volatile, while domestic cotton prices remain sensitive to crop and speculative factors. Furthermore, geopolitical disruptions can affect downstream demand, transit times, and freight costs. Therefore, while FY27 appears favourable, sustainability beyond the year will depend on Chinese demand trends, cotton price movements, geopolitical developments, pace of benefits from trade agreements, and the extent to which current spread recovery translates into sustainable PBILDT margin expansion across the value chain.

CareEdge Ratings View

The Indian cotton yarn industry has entered FY27 with its strongest operating environment in nearly three years, supported by a combination of factors, including structural supply rationalisation, improving export demand, and restoration of India's cost competitiveness in global markets. The exit of a meaningful portion of inefficient spinning capacity has strengthened the industry demand–supply balance, creating a more favourable backdrop for capacity utilisation levels and pricing. "The recent recovery differs from previous cyclical upswings as it is supported not only by demand improvement but also by a meaningful reduction in effective spinning capacity. This has improved the industry's pricing power and profitability outlook, particularly for organised and efficient players," says Akshay Morbiya, Associate Director, CareEdge Ratings.

While the near-term outlook remains favourable, the sustainability of the current upcycle will depend on the durability of export demand, particularly from China, the evolution of global apparel and home-textile consumption, and stability in cotton prices. Any significant divergence between domestic and international cotton prices, or a

resurgence of geopolitical and trade-related disruptions, could impact competitiveness and profitability. Consequently, the industry appears well-positioned for earnings recovery in FY27, although the extent to which the current improvement translates into a sustained multi-year growth cycle remains a key monitorable.

"The industry is witnessing a healthier operating environment driven by structural supply correction and improved demand conditions. While FY27 is expected to benefit from stronger spreads and better profitability, sustained growth will depend on the industry's ability to maintain global competitiveness and navigate demand volatility in key export markets," says Krunal Modi, Director, CareEdge Ratings.

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