THE CONSERVATIVE Shri Paul Oswal, chairman and MD of Vardhman Textiles, says no to risk.

WHY IT PAYS TO BE CONSERVATIVE

VARDHMAN TEXTILES' SHRI PAUL OSWAL STAYED AWAY FROM TAKING RISKY BETS DURING THE BOOM YEARS. THAT'S PAYING OFF NOW, AS THE STOCK HAS CONSISTENTLY OUTPERFORMED ITS PEERS.

BY ASHISH GUPTA

Photographs by **RONJOY GOGOI**

WHEN THE MOST ADMIRED rankings were released, and Vardhman Textiles had moved up the sector rankings (from 8 last year to 2 this year), there were plenty of wisecracks about spinning yarns and weaving stories. And then we took a look at the company's performance over the past one year, and all the funny stuff was forgotten. This is a company that's serious about yarns, whether spinning it or weaving it into fabric.

Its two factories, one in Budhni in Madhya Pradesh and the other in Baddi in Himachal Pradesh, produce nearly 110 million metres of fabric a year. Vardhman Acrylics, a sister company, has a polyester staple fibre factory in Bharuch in Gujarat, which has an installed capacity of producing 18,000 tonnes a year.

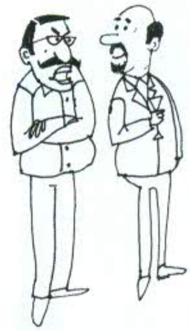
Despite various estimates that reckon that the textile industry can grow from $60 billion (Rs 3.6 lakh crore) to $110 billion in the next five years, Shri Paul Oswal, chairman and managing director of Vardhman Textiles, and son of the founder, Lala Rattan Chand Oswal, has kept his ambitions rather modest.

In the next five years, he wants to grow his conglomerate from $1.1 billion to $1.5 billion with no plans of loading his balance sheet with higher debts for greenfield projects, or acquisitions either at home or abroad. "Growth in the textile industry will be constrained by a slowing domestic and global economy, contentious issues such as land acquisition, and shortage of skilled manpower," says Oswal, when asked why he was not aiming for much more.

"I can't afford to take any foolhardy risks because I have to nurture a family of 30,000 employees," he adds. This streak of conservatism is what saw Vardhman through the bad days of 2010-11, when several domestic textiles companies teetered on the verge of bankruptcy.

Cotton prices had crashed to $1.5 a pound after touching a high of $2.5 a year earlier. Companies were stuck with high-priced inventories, and could not even export because of a government ban on cotton exports. Debts mounted to more than Rs 12,000 crore and several companies were forced to enter corporate debt restructuring schemes. Vardhman came through this crisis relatively better than most of its peers as it was a diversified company, making yarn, thread, and

FOR ITS GLOBAL CUSTOMERS, VARDHMAN FOCUSSES ON HIGH-END TEXTILES, WHICH MEANS HIGHER PRICES AND BETTER MARGINS.



fabric. Its conservative business approach also helped.

The market evidently likes this diversification. Most of the major brokerages have a "buy" recommendation on the stock, which trades at Rs 260 levels, way ahead of competitors Arvind Mills (Rs 78) and Bombay Dyeing (Rs 57). It looks like the market is seeing something right about Vardhman's future. In its February 2013 report, ICICI Securities said that Vardhman's yarn division will continue to grow on the back of strong exports to China, where cotton prices have soared due to government policies, making it unviable for Chinese spinners to manufacture cotton yarn. So most Chinese spinners will turn to India for cotton yarn.

An analyst at a Delhi-based brokerage who asked not to be named says the market here is bullish on textiles companies. "The devaluation of the rupee, firm demand from China, a potential easing of import norms by the European Union once the Free Trade Agreement is signed, and decent demand in the U.S. will increase textile companies' revenues in the second half of the current fiscal," he says.

Traditionally, textile firms do well in the second half of the year, thanks to a rise in demand at home, largely due to festivals, and increased buying in the U.S. and Europe.

Like it doesn't rely on just one product or segment, Vardhman doesn't rely on just one market, which also the street appreciates. Exports account for a chunk of revenue for textile companies. A report by the India Brand Equity Foundation, a trust established by the Department of Commerce under the Ministry of Commerce and Industry, states that the textile industry contributes about 14% to industrial production, 4% to gross domestic product (GDP), and 17% to export earnings.

While Vardhman, like its peers in the industry, exports a bulk of production, it pays a lot of attention to the domestic market. Thread, for instance, is almost entirely made for the domestic market. When it comes to fabric, exports account for up to 40% of output, and the company customises material for its big customers. "Our fabric collection for Gap (U.S.) will be different from that for Uniqlo (Japan) or s.Oliver (Germany) because different retailers cater to different segments of society," says Oswal.

For its global customers, Vardhman focusses on the high end of the textile chain, which means higher prices as well as better margins. For instance, it provides fabric that costs $250 a metre to a Japanese customer, Tejin. Vardhman is a preferred supplier to global garment makers such as Tommy Hilfiger, Esprit, Gap

(including brands such as Old Navy), Zara, H&M, Mango, Benetton, and Arrow. Japanese clothing retailer, Takisada, has chosen Vardhman as its fabric developer.

B.K. Choudhary, manager of Vardhman Textiles' Budhni factory, and managing director, Vardhman Acrylics, says that the company is now "trying to be an integral part of the fashion world, a part of the conversation". That's key to the company's plans for growth, and the reason why Vardhman's scientists and designers work so closely with customers and even retailers. That's how they understand what's happening in the world of fashion.

VARDHMAN MAY NEVER feature on any list of hot new design houses, but it's more than likely that such design houses use Vardhman's yarn, thread, or fabric. And this is the business that Oswal wants to grow. The business is important enough for the company to dedicate close to 1,500 sq. m. in the Baddi factory to research and development. Called the Central Product Development Cell, this unit is seen within the group as one of the most important, well, threads, in the fabrics business.

The unit is staffed by 10 full-time designers as well as a group of Italian designers who visit India every two months. Armed with the latest in CAD/CAM (computer-aided design and computer-aided manufacturing) software, the team is constantly developing new designs, new finishes, and what Choudhary calls "newer finishes of fabric", where different yarns are interwoven to create new varieties of fabrics.

FASHION TALK B.K. Choudhary, manager of Vardhman's Budhni factory, is pushing new kinds of fabric.

THE GROUP STRUCTURE

#In collaboration with Amercian & Efrid; *Recently started; Source: Company

It also creates fabric on demand. For instance, the team worked with Japanese garment maker Takisada-Osaka, to make what Oswal calls "a rare, expensive, and exotic variety"—a blend of modal (a synthetic fibre of the rayon family), silk, and wool. "A lot of collaboration and iterative effort goes into developing new fabrics, and global players rate our creativity quite highly," says Choudhary.

The design team is encouraged to visit exhibitions and fashion expos in France and Italy to study the latest fashion trends. Oswal says this is essential in order to meet the increasingly sophisticated demands of customers. Some of Vardhman's customers change their lines every month, so demand for fabric and yarn is always shifting with seasonal and fashion trends.

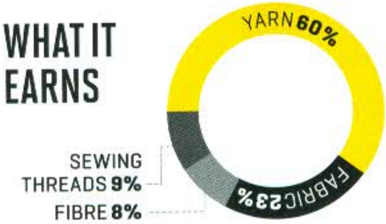
Today, Vardhman produces a wide range of fabric, yarn, and thread—from acrylic and hand-knitted cotton to Lycra, polyester, nylon, and every imaginable mix of these. Oswal believes that creating unique product lines is what will differentiate Vardhman from Raymond and Bombay Dyeing, and get it a premium. "Even a 2% to 3% premium is very good because the fabric business is so commoditised today," says Oswal.

Apart from R&D, Vardhman knows that to stay successful as an exporter, the company needs an efficient supply chain system. "Today, no garment manufacturer will wait for more than 45 days for delivery, because it only has around 90 days to meet its deadline of delivering to global retailers," says Choudhary. He explains that Vardhman has sourced top-of-the-line equipment from Benninger of Switzerland, Mondford of Germany, and Tsudakoma of Japan, to ensure that delivery does not get held up due to mechanical problems.

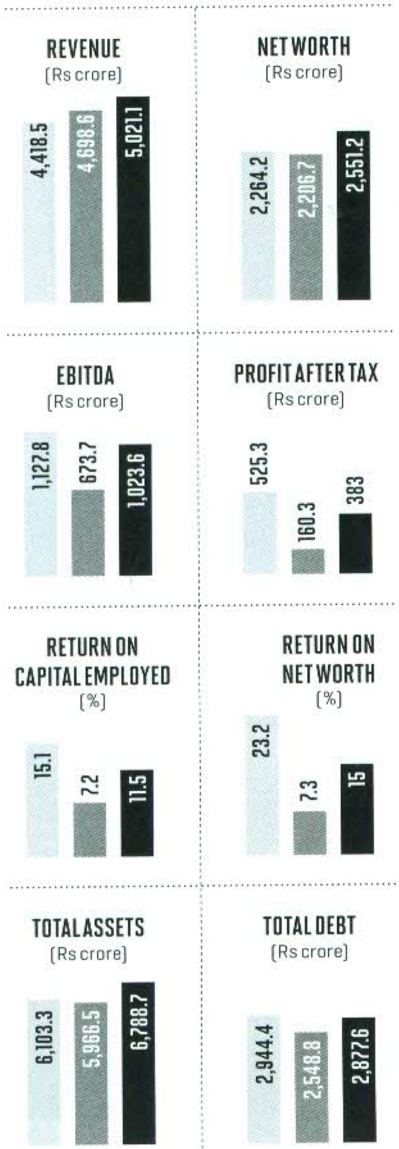
Anup Thatai, CEO, Orient Craft, a Rs 1,500 crore garment export company based in Gurgaon, has only good things to say about Vardhman. Orient buys raw material (yarn and fabric) worth up to Rs 250 crore every year from Vardhman. "The best thing about Vardhman is the consistent quality of its products, so important for an export-oriented company like ours," says Thatai. "We also work with it in developing fabrics and can confidently say it has kept up with the latest developments in fashion and technology."

Vardhman sells to exporters such as Thatai, and factories in Sri Lanka and Bangladesh, which make garments for export to countries like the U.S. The company's foreign exchange cell, managed by the chief financial

WHAT IT EARNS



KEY FINANCIALS



FY11 ● FY12 ● FY13 SOURCE: COMPANY

officer and an executive director, helps manage currency risks. At the same time, a fall in textile demand in developed countries could affect sales. Last year, there was a sharp fall in demand for textiles in the U.S. and Europe, which hit Vardhman's yarn and fabric export.

In his letter to shareholders in the company's 2011-12 annual report, Oswal wrote: "Due to the lower-than-average growth in these years [2008 to 2011], the consumption of fibre in the world has not increased. Cotton consumption is expected to come down... This is attributable to poor offtake in large-consumption economies like the U.S. and Europe... Altogether I can only predict there will be unrelenting pressure on margins in the industry."

For FY12, Vardhman Textiles reported a profit of Rs 109.7 crore, compared with Rs 469.7 crore the previous fiscal.

THE GOOD NEWS is that there are signs of a revival in the industry, says Ajay Srinivasan, director, Crisil Research, a Mumbai-based research house. "This year is far better than the last," he says. "Even the U.S. market saw a 7% jump in imports in the January-March quarter this year compared to a flat growth last year."

Arvind Singhal, chairman of consulting firm Technopak, says Vardhman is well-placed to gain from the current revival in the textile sector. "China is the biggest player in the textile market, but its production has reached its peak, and growth in the sector is slowing. Also, because of government policies, Chinese cotton has become very expensive. Compounding the problem is the increased labour cost. There is also a rising domestic demand, which is slowing exports," says Singhal.

Oswal too is confident that Vardhman will not suffer even if global demand slows. The threads division of the company exports little; the bulk of its production is sold in the domestic market. "We are one of the few players to survive the onslaught of Coates India in the 1980s. We are the second-largest thread producer in the country in a business that is littered with failed players such as Delhi Cloth Mill and Calico," says Oswal.

Today, the threads business produces 75,000 varieties of thread and has a 30% share of the market compared with Coates's 35%, and announced a revenue of Rs 546.3 crore in 2011-12. Vardhman thread is sold under the American & Efrid brand, and covers a wide range of users, from tailors to kite-flying enthusiasts, to beauty salons, and automobile seat manufacturers. "You name it and we are there," says Oswal proudly.

Oswal believes that the way to leadership is "through excellence, not rank and size". That said, Vardhman is the only textile player in India which resembles Chinese players in terms of size. "There are only two or three companies in China, which are in the $2 billion to $3 billion club," says Oswal.

He says his greatest achievement has been to create a strong homegrown leadership team—both his managing directors have been with him from 1973—and become a respected player in the global textile industry. "It was Arvind [Mills, set up by the Lalbhai brothers in the 1930s] which showed the way, and we followed," he says. Now, it's his turn to show the way.

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