



Upgrading estimates

We are upgrading our earning estimates for all the cement companies under our coverage for FY07, FY08 and FY09 to factor in the higher price hikes expected in 4QFY07 and FY08. Our estimates factor in a price increase of Rs5/bag QoQ in 3QFY07 and Rs7.5/bag QoQ in 4QFY07. Also, our FY08E estimates assume a price that is Rs5/bag higher in FY08E compared with FY07E average prices, and Rs5/bag decline in FY09E over FY08E average prices. As a result, our estimates have increased by 1%-3% for FY07E, 10%-17% for FY08E and 12%-25% for FY09E. We believe there is strong probability of higher price hikes in 4QFY07, when construction activity is at its peak. As effective capacity utilization would remain above 90% even in FY09, any positive surprises in demand or delay in capacity addition would not only prolong the upturn in cement cycle further, but in the interim also enhance pricing power of producers.

REVISED FORECASTS

	FY07E EPS (RS)			FY08E EPS (RS)			FY09E EPS (RS)		
	NEW	OLD	CHG (%)	NEW	OLD	CHG (%)	NEW	OLD	CHG (%)
ACC	61.1	61.1	0.0	79.3	69.0	15.0	73.5	62.3	18.0
Grasim	209.3	206.7	1.2	230.9	210.3	9.8	232.1	203.7	13.9
Gujarat Ambuja	9.6	9.6	0.0	12.2	11.1	10.4	11.7	10.4	12.4
UltraTech	65.2	63.8	2.2	79.7	68.2	16.9	87.2	74.7	16.7
Birla Corp	40.4	39.4	2.7	48.7	42.3	15.2	46.3	38.2	21.2
Kesoram	62.4	61.6	1.3	81.1	73.3	10.6	83.5	74.6	12.0
Shree Cement	95.4	94.3	1.1	136.2	122.8	10.9	157.1	125.7	24.9

Source: Motilal Oswal Securities

Capacity utilization to remain >90% in FY09

Although up to 72-75m ton of capacity addition has been already announced, meaningful capacity addition would be operational only by end-FY08 and in FY09 (assuming no delays). However, adjusting for non-operative capacity (~5.5m ton) and timing of capacity additions after taking into account likely delay, effective capacity utilization for FY07E, FY08E and FY09E would be 99%, 100% and 93% respectively. Even if we do not factor in any delay, capacity utilization for FY08E and FY09E would be around 99% and 92% respectively.

SUPPLY-DEMAND DYNAMICS (M TON)

	FY04	FY05	FY06	FY07E	FY08E	FY09E
Cement Capacity (Year end)	146.2	153.8	160.3	171.4	194.8	233.6
Clinker Exports	5.6	6.0	3.2	3.3	3.3	3.3
Cement Dispatches (incl exports)	117.1	125.1	141.6	155.6	170.2	186.0
Growth (%)	5.5	6.8	13.2	9.9	9.4	9.3
Capacity Util (incl clinker exports)	84.3	85.5	90.5	92.9	89.2	81.1
Effective Cap *	138.7	146.3	154.8	161.0	173.7	203.9
Effective Cap Util (%)	88.9	89.9	93.7	98.9	100.0	92.9

*Effective capacity is adjusted for non-operative capacity and is the quarterly add-up of capacity additions after taking into account likely delay in capacity additions. Source: CMA/Motilal Oswal Securities

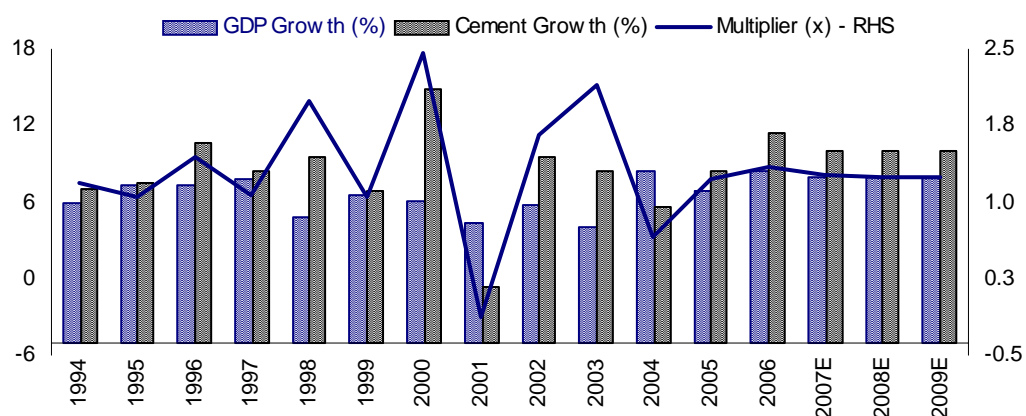
Also, we note the new capacities would take around 3-6 months to stabilize operations, which would further push back impact of these new capacities, resulting in prolonging the current upturn in the cement cycle. The ongoing upturn in the cement cycle is expected to be sustained at least for a further 18 months (to 2QFY09), translating into a strong pricing environment in the interim.

Possible positive surprises in demand and supply

Our estimate factors in 10% CAGR in demand over FY06-09E (but does not factor in any delay in capacity addition). However, we believe the following triggers can lead to positive surprises in terms of both demand and supply, which can extend the cement cycle upturn over a longer period:

- Economic environment conducive for robust cement demand:** Historically, cement dispatches have grown at around 8% and have exhibited a strong correlation with GDP growth (~1.25x multiplier). However, with GDP growth expected to sustain at >8%, there exists strong possibility of cement demand exceeding 10%. The government's focus on infrastructure building augurs well for cement demand growth exceeding 10%.

TREND IN CEMENT AND GDP GROWTH



Source: CMIE, CMA/ Motilal Oswal Securities

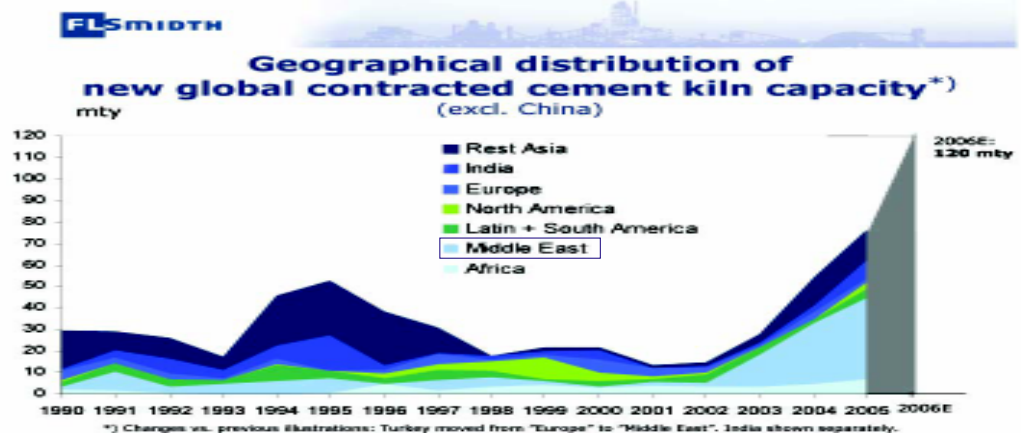
CAPACITY UTILIZATION: SENSITIVITY TO DEMAND GROWTH

DEMAND GROWTH (%)	CAPACITY UTILIZATION (%)		
	FY08E	FY09E	FY10E
8.0	97.8	90.2	86.8
10.0	99.5	91.8	88.4
12.0	101.2	93.4	89.9
14.0	102.9	95.0	91.4

Source: Motilal Oswal Securities

- Capacity additions later than expected:** Although the announced capacity addition is around 72m-75m ton (refer Annexure), our interaction with industry sources suggests that there is unexpected delay in adding capacity. This delay is due to: (a) a huge order backlog with cement equipment suppliers; and (b) delay in regulatory clearances and land acquisition. Consequently, a majority of the new capacity additions would not be operational before 2HFY09, the full impact of which would only be felt in FY10.

GEOGRAPHICAL DISTRIBUTION OF NEW GLOBAL CONTRACTED CEMENT CAPACITY

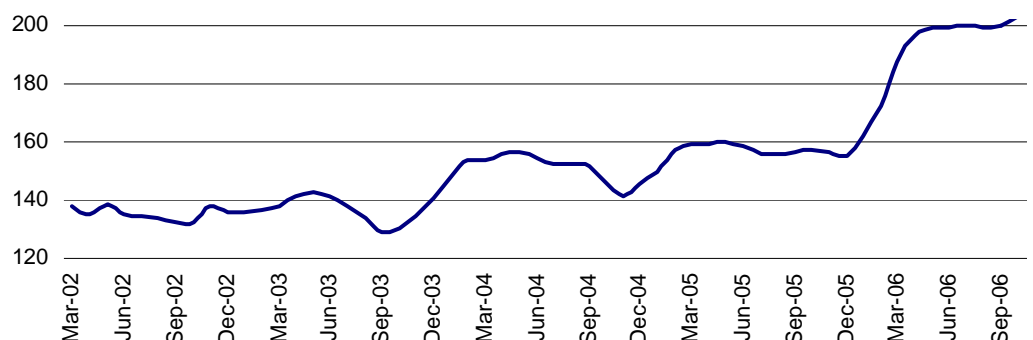


Source: FLSmidth

Pricing environment to remain favorable

Higher volume growth and limited capacity addition has improved the supply-demand scenario significantly. This is reflected in around 27% YoY higher prices in 1HFY07. Pricing momentum is expected to continue, as witnessed in the price hike of Rs4/bag QoQ in 2QFY07 (despite the monsoon quarter) and another Rs3-5/bag price hike across India (except southern India) from November 2006. High capacity utilization and strong demand growth could lead to some short-term deficit for cement during January-June 2007 as construction activity gathers full momentum. This could lead to higher-than-expected price hikes during this period. Our estimates factor in a price increase of Rs5/bag QoQ in 3QFY07 and Rs7.5/bag QoQ in 4QFY07. Also, our FY08E estimates assume a price that is Rs5/bag higher in FY08E compared with FY07E average prices, and Rs5/bag decline in FY09E over FY08E average prices.

TREND IN NATIONAL AVERAGE CEMENT PRICES (RS/50KG BAG)



Source: CMA/Motilal Oswal Securities

Stocks to follow earnings upgrades

In line with our upgrade in earnings estimates for cement companies under our coverage universe and our positive view on the sector, we have raised our target prices. We value the large caps at 13x-14x FY08 EPS and mid caps at 10x-12x FY08 EPS. Amongst the large caps, we prefer **Gujarat Ambuja** and **Grasim**. Within the mid-caps, we like **Kesoram**, **Birla Corporation** and **Shree Cements** at the current levels.

COMPARATIVE VALUATION

VALUATIONS	CMP		TARGET PRICE	EPS (RS)			P/E (X)			EV/EBITDA (X)			EV/TON (US\$)-CAP			EV/TON(US\$)-PROD		
	(RS)	RECO		FY07	FY08	FY09	FY07	FY08	FY09	FY07	FY08	FY09	FY07	FY08	FY09	FY07	FY08	FY09
ACC *	1,105	Neutral	1,111	61.1	79.3	73.5	18.1	13.9	15.0	12.6	9.1	9.1	222	210	187	242	216	187
Birla Corp.	337	Buy	490	40.4	48.7	46.3	8.3	6.9	7.3	4.7	3.6	3.6	91	83	60	96	82	65
Grasim	2,758	Buy	3,000	209.3	230.9	232.1	13.2	11.9	11.9	8.3	7.3	7.3	220	208	133	216	204	163
Gujarat Amb.	141	Buy	172	9.6	12.2	11.7	14.7	11.5	12.1	10.2	7.3	7.3	264	261	188	250	227	198
Kesoram	543	Buy	815	62.4	81.1	83.5	8.7	6.7	6.5	5.9	4.5	4.5	101	96	64	130	103	81
Shree Cem.	1,396	Buy	1,635	95.4	136.2	157.1	14.6	10.2	8.9	8.7	5.8	5.8	194	119	94	258	179	126
UltraTech	957	Buy	1,115	65.2	79.7	87.2	14.7	12.0	11.0	8.4	7.0	7.0	163	150	115	161	143	124
Sector Agg.							14.4	11.3	11.5	9.4	7.0	6.5	190	167	122	189	165	138

*Year ending December

Source: Motilal Oswal Securities

ANNEXURE I: DETAILS OF ANNOUNCED CAPACITY ADDITION BASED ON THE COMPANY'S INDICATIONS (M TON)

COMPANY/PLANT	FY07E				FY08E				FY09E			
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q
ACC	0.9											
Dalmia Cement	2.3											
JK Cement (JK Syn)	0.5											
JP India	0.5											
OCL India	0.5											
ACC		0.9										
JK Lakshmi Cement		0.2										
Lafarge		0.4										
Ultratech Cemco - All plants		0.5										
Kesoram Ind			1.6									
Sanghi Ind.			0.6									
Gujarat Ambuja				1								
Shree Cement				1.5								
Gujarat Ambuja					1							
Binani Ind-Sirohi						3.1						
Gujarat Ambuja						0.5						
Grasim - Dadri						1						
Madras Cement						2.0						
Mangalam Cement							0.5					
Shree Cement							1.5					
Shree Cement							2.0					
JP Ind - HP							3	1				
Birla Corp								0.6				
India Cement								2.0				
JP Ind - Gujarat Anjan								1.2				
JP Ind - Siddhi								1.5				
JP Ind - UP cement								2.5				
Grasim									4.0			
Madras Cement									2.0			
Zuari Cement									2.5			
ACC										1.0		
Birla Corp											0.6	
Century Textile											2.0	
Century Textiles											1.5	
Gujarat Ambuja											2.3	
India Cement											2.0	
JK Lakshmi Cement											1.0	
JP-SAIL											0.5	
JP-SAIL											2.0	
Kesoram Ind											1.6	
OCL India											2.3	
Shree Cement											1.5	
Ultratech Cemco											4.0	
Grasim												4.0
JK Cement												3.0
Orient Papers												1
Total	4.7	2.0	2.2	2.5	1.0	6.6	7.0	8.8	8.5	1.0	21.3	8.0
Total Capacity (Year End)				171.4				194.8				233.6
Total Despatches				159.1				173.7				189.5
Capacity Utilization (%)				93				89				81
Effective Cap*				161.0				174				204
Effective Cap Util (%)				99				100				93

*Effective capacity is adjusted for non-operative capacities and is monthly add-up of capacity additions after taking into account likely delay in capacity addition.

Source: Motilal Oswal Securities

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