Cement

Sector Update

Strong demand continues in North and South

In February 2008, cement industry recorded sales of 14.72 million metric tonne (MMT) against 13MMT in February 2007, thereby registering a growth of 13.2% year on year (yoy). On a year-to-date (Y-T-D) basis, the industry posted a growth of 7.7% and sold 150.56MMT of cement during 2007-08.

Strong demand absorbs supply

To give a view of the demand scenario, we have highlighted the following key points:

- Capacity utilisation in North India was at 104% and dispatches were more than what was produced for the second consecutive month, implying lower stock levels with the companies. Also looking at the Y-T-D numbers we see that the northern region has grown more, both in terms of production and dispatches, clocking a growth of over 12%.
- Capacity utilisation in West India was at 105%. However dispatches were less than production implying some stock build-up with the manufactures in the region.
- Capacity utilisation in South India was at 99% and dispatches were more than production leading to lower stock levels. The companies operating in this region achieved a Y-T-D growth of over 9% both in production and dispatches.
- Capacity utilisation in East India was at 94%. However more cement was sold than produced implying some reduction in stock levels. Lower capacity utilisation rate on a Y-T-D basis implies that demand is not as robust as is in the other parts of the country.
- Central region also saw a 102% capacity utlisation rate, though production was almost equal to dispatches.

Regison-wise dispatches for February 2008

Particulars	Feb 2008	Feb 2007	% chg	YTD 2008	YTD 2007	% chg
North						
Production	3.15	2.52	24.9	32.76	29.12	12.5
Dispatches	3.17	2.45	29.3	32.73	29.03	12.7
Capacity utilisation	104%	93%		102%	99%	
West						
Production	2.54	2.47	2.8	26.0	24.7	5.2
Dispatches	2.49	2.45	1.6	25.9	24.7	4.8
Capacity Utilisation	105%	102%		98%	93%	

Particulars	Feb 2008	Feb 2007	% chg	YTD 2008	YTD 2007	% chg
South						
Production	4.69	4.16	12.6	49.10	44.95	9.2
Dispatches	4.71	4.28	10.1	49.03	44.95	9.1
Capacity Utilisation	99%	93%		96%	91%	
East						
Production	2.05	1.88	9.2	20.81	19.83	4.9
Dispatches	2.10	1.91	10.0	20.78	19.78	5.1
Capacity utilisation	94%	90%		88%	87%	
Central						
Production	2.24	1.96	14	22.56	21.76	3.7
Dispatches	2.25	1.91	18	22.11	21.33	3.7
Capacity utilisation	102%	92%		95%	93%	

Among the large-cap stocks, ACC recorded the highest year-on-year (y-o-y) increase of 19% in cement dispatches, as three of its plants were undergoing technical modification that affected the production during the corresponding period last year. As a result ACC could sell only 1.42MMT during February 2007 and sold 1.69MMT during February 2008. Grasim Industries also recorded a 10% growth in dispatches and sold 1.39MMT cement.

Amongst the Sharekhan mid-cap universe, Shree Cement reported the highest dispatch growth of 71.1% to 0.65MMT mainly on account of a 1.5 million tonne per annum (MTPA) cement capacity going on stream and a 2MTPA grinding unit getting operational during the current fiscal. Orient paper reported a growth of 17.6% to 0.2MMT, while Madras cement reported a growth of 17% to 0.48MMT.

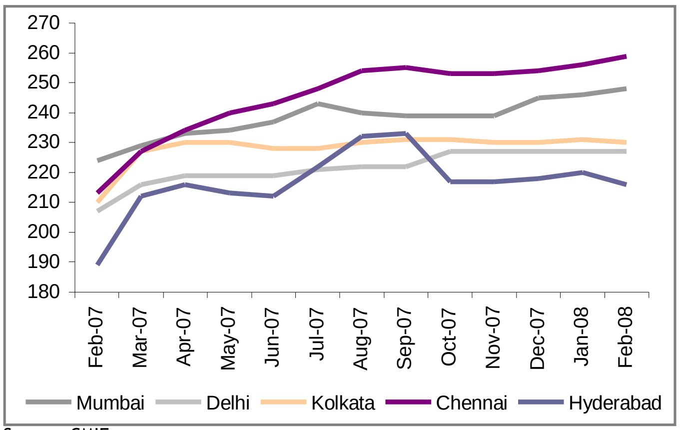
We expect the cement industry to sustain high volumes in March, as the construction activity is at its peak during the month, traditionally. As far as cement prices are concerned, metros saw some increase in prices. Comparing sequentially, we have seen that during February 2008, Mumbai witnessed an increase of Rs2 a bag to Rs248, and in Chennai the prices strengthened by Rs3 to Rs259 a bag. In Hyderabad the prices declined by Rs4 to Rs216 a bag. On year-on-year basis prices were up by 22% in Chennai, 14% in Hyderabad, 11% in Mumbai and 10% in Delhi and Kolkata. The movement in wholesale price index (WPI) of cement indicates that on an average cement prices in India were up by 9% yoy. Apart from this, in March bulk cement prices went up by Rs4-8 per bag, reflecting the hike in the excise duty, as announced in the Union Budget 2008-09.

Cement prices for 50 kg bag (Rs)

City	Feb 2008	Feb 2007	% yoy chg	Jan 2008	% mom chg
Mumbai	248	224	11	246	1
Delhi	227	207	10	227	0
Kolkata	230	210	10	231	0
Chennai	259	213	22	256	1
Hyderabad	216	189	14	220	-2

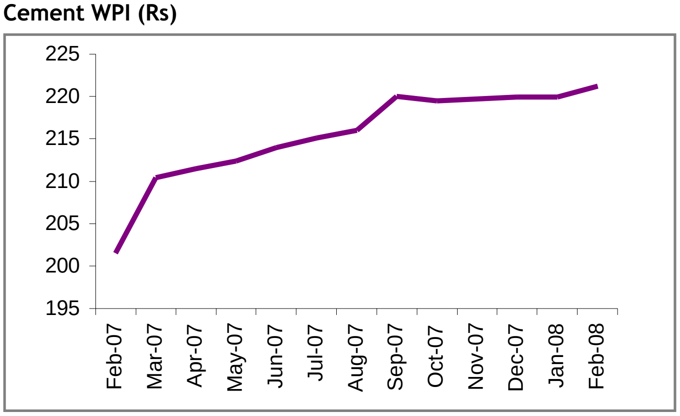
Source: CMIE

Cement prices in major cities



Source: CMIE

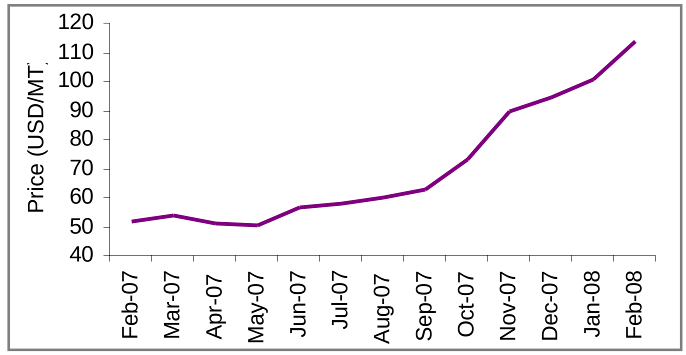
Cement WPI (Rs)



Source: Bloomberg

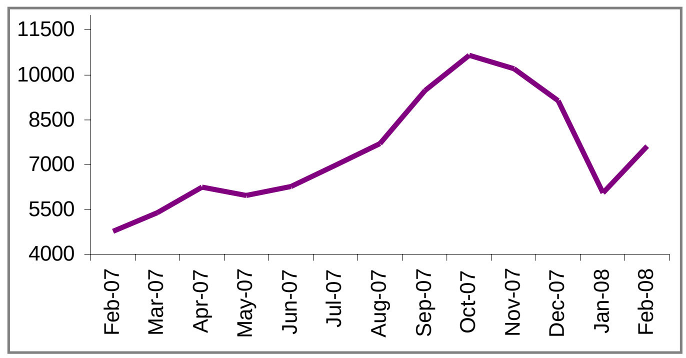
On the cost front, cement industry witnessed a sharp increase in fuel prices. The price of South African coal in February 2008 was up 121% yoy to USD114 per metric tonne. The landed price of International coal has also increased due to an increase in the freight rates. The Baltic dry Index was up by 60% yoy in February 2008. Players such as India Cement, bulk of whose requirement is met by imported coal, has purchased two ships and is on the lookout for opportunities for investment in coal mines abroad. Domestic prices of coal have increased by 10-15%. The prices of domestic pet coke were also up by more than 30% yoy. Cement manufacturers use pet coke and coal as fuel in kiln and for firing their captive power plants. Madras Cement is increasing its wind power capacity to protect it self from high fuel prices. JK Cement will also commission a 13 mega watt waste heat recovery plant to keep a check on its fuel bills.

South African coal export prices (USD/MT)



Source: Bloomberg

Baltic dry Index



Source: Bloomberg

Going ahead, with crude hovering around USD110 a barrel and Indian basket also close to USD105 a barrel, there is an up ward bias towards the prices of pet coke and diesel. Increase in domestic diesel prices will lead to an increase in the freight cost, which will worsen the cost concern of the industry.

Outlook

Higher budget allocation for infrastructure spending would lead to strong demand for cement industry. In the Union budget 2008-09, allocation for Bharat Nirman has been increased by 27% to Rs31,280 crore, while the allocation for National Highway Development Project (NHDP) has been raised by 19.3% to Rs12,966 crore. However on the flip side, in the long run the demand from another user industry, real estate, may see a slow down due to concerns relating to affordability. Also, about 75-80% of demand for office space and 40% of demand for residential space is generated by Information Technology (IT)/IT enabled services (ITES) sector. Currently, IT firms are struggling to get a better clarity of the IT budgets of their clients for the calendar year 2008.

Unlike the past when the key driver for the earnings of cement companies were prices, we believe that volumes and cost saving will drive the earnings of the cement industry in FY2009. Some of the players that have added new capacities in the recent past are Shree Cement, Orient Paper and Madras Cement. Whereas, companies like Grasim and UltraTech are in the process of commissioning new capacities shortly.

Company-wise dispatches for February 2008

Company	Feb-08	Feb-07	% yoy
ACC	1.69	1.42	19.0
Ambuja Cement	1.46	1.36	7.4
UltraTech	1.33	1.32	0.8
Grasim	1.39	1.26	10.3
Jaiprakash Associates	0.61	0.60	1.7
Orient Paper	0.20	0.17	17.6
Madras Cement	0.48	0.41	17.1
India Cement	0.82	0.77	6.5
JK Cement	0.29	0.29	0.0
Shree Cement	0.65	0.38	71.1
Industry	**14.72**	**13**	**13.2**

The author doesn't hold any investment in any of the companies mentioned in the article.

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Housing Development Finance Corporation
HDFC Bank
Infosys Technologies
Larsen & Toubro
Reliance Industries
Tata Consultancy Services

Apple Green

Aditya Birla Nuvo
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Bajaj Auto
Bank of Baroda
Bank of India
Bharat Bijlee
Bharat Electronics
Bharat Heavy Electricals
Bharti Airtel
Canara Bank
Corporation Bank
Crompton Greaves
Elder Pharmaceuticals
Grasim Industries
HCL Technologies
Hindustan Unilever
ICICI Bank
Indian Hotels Company
ITC
Mahindra & Mahindra
Marico
Maruti Suzuki India
Lupin
Nicholas Piramal India
Punj Lloyd
Ranbaxy Laboratories
Satyam Computer Services
SKF India
State Bank of India
Tata Motors
Tata Tea
Unichem Laboratories
Wipro

Cannonball

Allahabad Bank
Andhra Bank
Gateway Distriparks
International Combustion (India)
JK Cement
Madras Cement
Shree Cement
Tourism Finance Corporation of India

Emerging Star

3i Infotech
Aban Offshore
Alphageo India
Axis Bank (UTI Bank)
Balaji Telefilms
BL Kashyap & Sons
Cadila Healthcare
Jindal Saw
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Navneet Publications (India)
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Aurobindo Pharma
BASF India
Ceat
Deepak Fertilisers & Petrochemicals Corporation
Genus Power Infrastructures
ICI India
India Cements
Indo Tech Transformers
Ipca Laboratories
Jaiprakash Associates
KEI Industries
Mahindra Lifespace Developers
Mold-Tek Technologies
Orbit Corporation
Punjab National Bank
Ratnamani Metals and Tubes
Sanghvi Movers
Selan Exploration Technology
SEAMEC
Shiv-Vani Oil & Gas Exploration Services
Subros
Sun Pharmaceutical Industries
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