

# CEMENT

*Pricing weakness sets in; time to lighten positions in frontliners*

Continuing the tepid trend witnessed in February, overall cement despatches grew only 8.4% in March 2010 (taking FY10 demand growth to 10.4%). With logistic problems having eased, prices have come off / expected to come off in most regions, except South. As the sector will enter a seasonally weak monsoon quarter amidst new capacity additions and cost pressures, we recommend booking gains in largecaps.

## ■ Dealer interactions reflect subdued demand; price upticks ruled out

At the ground, strong demand situation witnessed in December /January FY10 has eased. In the **North**, while prices in Lucknow have corrected by ~INR 50/bag in the last one month (INR 250-270/bag for retail; INR 225-235/bag for project), prices in Delhi too remain under pressure. Project demand is likely to taper down in a month's time with reduced offtake from the Commonwealth Games. Lead time for material delivery has shrunk to 4 days from 10 days in February. While prices in the **West** are holding on, this is due to curtailed supply from the South. In the **East**, dealers were concerned about offtake and cited weakness in retail demand. While prices are stable at present, correction is imminent. Also, enquires to other regions from North and East have come off.

## ■ South pricing on a roll; party to last only till monsoon

Power shortage remains acute in Andhra Pradesh (3-7 days/month) and has helped producers to restore demand-supply equilibrium. Prices are up to INR 210-225/bag in Hyderabad. Interestingly, prices in other states like Tamil Nadu have also shot up to ~INR 260/bag levels. Interaction with market participants reflect that current hikes are opportunistic and discipline is unlikely to last in monsoon.

## ■ Cost pressures mounting; impact to accentuate ahead

Despite average price hike of INR 30-80/bag in Q4FY10 from the lows of Q3FY10, improvement in EBITDA margin will not be in tandem due to sharp increase in input costs. Going ahead, impact of rise in imported coal rates, 11% hike in domestic coal, increase in freight cost with hike in diesel rates and removal of service tax exemption on rail freight will further play out. Also, players will need to bear the increase in excise duty, which they were able to pass on until recently.

## ■ ~48mtpa capacity addition in FY10; majors adding 13.5mtpa in Q1FY11E

While installed capacity addition for FY10 stood at 48 mt, effective addition was only 29 mt, implying that full impact is yet to come. Also, for Q1FY11, the industry is likely to add ~19 mt, of which, 13.5 mtpa will be added by majors.

## ■ Outlook: Lighten positions in frontliners

We believe valuations of frontline stocks like Ambuja, ACC, and UltraTech are expensive and investors must use current valuations as exit opportunity. Grasim continues to be our preferred stock within the coverage. Midcap stocks (not rated) which are currently trading at attractive valuations are Mangalam Cement (EV/t - \$54), Heidelberg Cement (EV/t - \$56), JK Cement (EV/t - \$48), JK Lakshmi Cement (EV/t - \$49) and Dalmia Cements. However, despite attractive valuations, these stocks will too get impacted by weakness in sector fundamentals and are likely to perform only incase of any inorganic trigger in the sector.

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**Table 1: Midcaps to watch out for**

	Heidelberg	JK Cement	JK Lakshmi	Mangalam cement	Dalmia Cement
Capacity (current)	3.1	7.5	5.6	2.0	9.0
Market cap (USD mn)	275	268	195	113	416
D:E	0.0	0.5	0.8	0.1	1.5
YTD EBITDA/t	622	1,108	1,014	1,211	1,095
EV/EBITDA (TTM)	4.1	3.6	1.6	2.5	7.3
EV/tonne	56	48	49	54	NA
P/BV	2.2	1.1	1.1	1.9	1.6

Source: Company, CMA, Edelweiss research

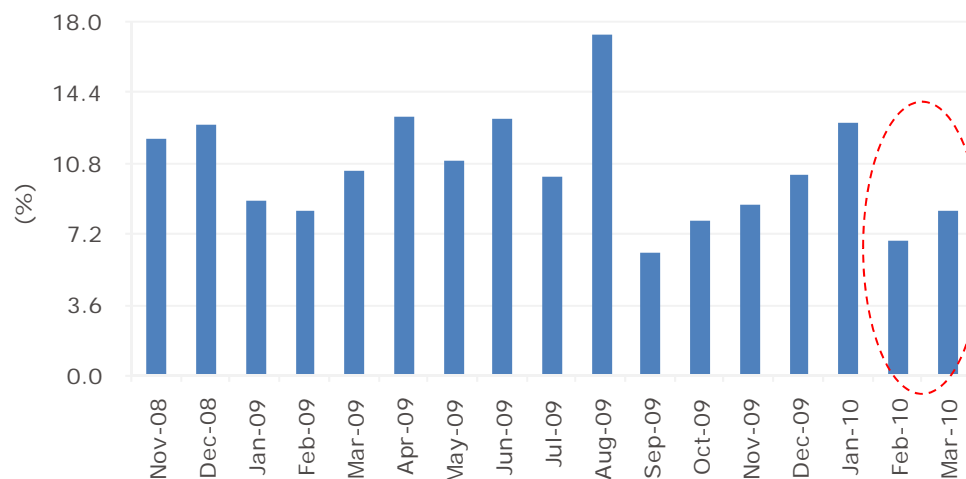
Note: Above calculations are based on last reported balance sheet details and prices as of 16th April, 2010

**March: Growth tepid for 2<sup>nd</sup> month in a row; FY10 despatch growth at 10.4%**

**Table 2: Cement despatch figure**

(Mn tonnes)	Mar-10	Feb-10	Mar-09	Change (Y-o-Y)	Change (M-o-M)	FY10	FY09	Change (%)
<b>Cement majors</b>	<b>10.3</b>	<b>8.9</b>	<b>9.0</b>	<b>14.4</b>	<b>15.2</b>	<b>101.7</b>	<b>90.3</b>	<b>12.6</b>
ACC	1.9	1.7	2.0	(3.5)	13.5	21.3	21.3	0.1
Ambuja Cements	1.9	1.7	1.7	11.6	13.6	19.2	18.0	6.8
AV Birla Group	3.7	3.2	3.4	9.8	15.2	37.0	32.3	14.6
Shree Cement	0.9	0.8	0.7	25.4	18.8	9.4	7.8	20.7
Dalmia Cement	0.4	0.4	0.4	15.2	14.5	4.1	3.4	20.6
Jaypee Group	1.4	1.2	0.8	75.1	17.9	10.7	7.6	40.4
<b>Others</b>	<b>9.4</b>	<b>8.2</b>	<b>9.1</b>	<b>2.5</b>	<b>14.3</b>	<b>97.9</b>	<b>90.5</b>	<b>8.1</b>
<b>All India</b>	<b>19.6</b>	<b>17.1</b>	<b>18.1</b>	<b>8.4</b>	<b>14.8</b>	<b>199.6</b>	<b>180.9</b>	<b>10.4</b>

Source: Company, CMA

**Chart 1: Y-o-Y despatch growth at 8.4% for March 2010**

Source: CMA

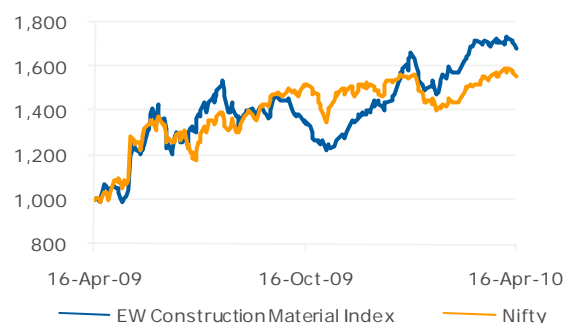
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### Coverage group(s) of stocks by primary analyst(s): Cement

ACC, Ambuja Cement, Grasim Industries, India Cements, Jaiprakash Associates and UltraTech Cement

#### EW Indices



#### Distribution of Ratings / Market Cap

##### Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	101	56	9	169

\* 3 stocks under review

	> 50bn	Between 10bn and 50 bn	< 10bn
Market Cap (INR)	103	53	13

#### Recent Research

Date	Company	Title	Price (INR)	Recos
16-Mar-10	Heidelberg Cement India	Much ignored turnaround; Visit Note	48	
04-Feb-10	Ambuja Cements	Dip in realisation dents PAT; Result Update	100	Hold
04-Feb-10	ACC	Favourable sales mix; Result Update	844	Hold
25-Jan-10	India Cements	Out of steam; Result Update	113	Reduce

#### Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

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