

Sector : Cement - An opportunity to buy

Indices as on 12th March		
	closing	PE Ratio
Sensex	12903	19.87
Nifty	3735	17.96
ET Cement	7937	10.95

ACC (2nd Jan to 9th March 2007)

Grasim Ind. (2nd Jan to 9th March 2007)

Guj Amb. (2nd Jan to 9th March 2007)


After the announcement of dual excise system in the union budget the cement industry and the Government engaged in a bitter battle.

Having concern of inflation in mind to curb the prices of some basic products including cement on one side on the part of government and to take the benefit of growing demand of product to encash the benefit by raising cement prices, the issue has become a hot topic and created uncertainty in the mind of investors, the result is that cement stocks have come down heavily.

The matter started first in last week of January, 2007 when Government reduced the import duty on cement to nil from 12.5%. This was an indication and message of Govt inclination to check the inflation in general and cement prices in particular.

We feel the tussle between Industry and Government has provided an opportunity for investors to pick good cement stocks now available at a discount of 20% to 30% from one month's peak prices as the outlook for Industry remains positive and current valuation attractive.

Chronology of the events concerned to industry is as under:

- A. 23 Jan, 2007:
Govt announces the removal of 12.5% duty on import of Cements
- B. 28 Feb, 2007:
Union Budget proposes dual system of Excise duty on Cement with reduction of duty from Rs 400 to Rs 350 on selling price up to Rs 190 per bag and Excise duty of Rs 600 on selling price above Rs190 per bag.
- C. 7 March, 2007:
Industry Minister Mr Kamal Nath gives statement indicating putting a ban on export of cement.
- D. 9 March, 2007:
Cement Industry agrees to freeze the price at current level and not to increase the price for one year and absorbing any increase in cost and passing on any sops to consumers.

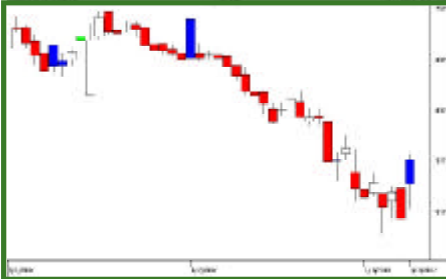
Reacting to these developments the cement stocks has corrected as under:

Scrips	CMP 12/3	PE	EPS(TTM)	CP 22/01	% Ch. on Event A	% Ch. on Event B	% Ch. on Event C	% Ch. on Event D	1 MONTH H/L(9/2 - 9/3)		
									H	L	CMP/1M H
1 ACC	747	12.8	58.3	959.85	-4.73%	-6.03%	-15.56%	-18.62%	1072	750	-30.3%
2 GUJ AMBUJA	105	12.4	8.5	146.85	-6.71%	-21.14%	-29.32%	-25.06%	143.15	100	-26.4%
3 GRASIM	2014	10.5	191.5	2909	-3.58%	-23.96%	-27.74%	-28.77%	2895	1932	-30.4%
4 INDIA CEMENT	155	10.2	15.2	241.8	-8.68%	-26.10%	-37.22%	-36.60%	222	147.1	-30.1%
5 JP ASSOCIATES	545	29.9	18.2	733.65	-2.66%	-25.61%	-30.50%	-24.82%	688	463	-20.8%
6 ULTRATECH	737	13.2	55.9	1118	-5.19%	-20.57%	-29.07%	-30.23%	1123	752	-34.4%

Ultratech (2nd Jan to 9th March 2007)



J P Asso. (2nd Jan to 9th March 2007)



India Cem. (2nd Jan to 9th March 2007)



Our recommendations to buy-

Large caps: ACC, Guj Ambuja, Grasim, Ultratech

Others : Shree Cements, India Cement, J K Cement, Rain Commodities

Positives:

- ✍ Demand of cement is growing around 10% and more.
- ✍ Govt focus on Infrastructure in Union Budget will continue the momentum of demand growth.
- ✍ At current selling price Industry is making handsome profit.
- ✍ Operating cost are not likely to increase substantially.
- ✍ Removal of import duty had no impact. Even after increase in Excise and consequently cement prices per bag, domestic cement is still cheaper by 5 to 7% from landed cost, if imported.
- ✍ Cement industry is making investment of about Rs 45,000 cr to increase the capacity by 100 mn tons and major supply is not coming before middle of FY09.
- ✍ All cement stocks have heavily come down from their recent peaks made in previous 1-2 months and are currently available at 20% to 30% lower levels.
- ✍ All major cement stocks are currently available at attractive PE ratio.
- ✍ Railway budget has announced to come out with a comprehensive package for transportation of cement.

Negatives:

- ✍ In an effort to curb the inflation Govt is trying and doing all efforts to curb the rising cement prices which is creating a fear of Govt Control in indirect way.
- ✍ The gap between domestic prices and landed cost has narrowed down, limiting the scope for further rise in domestic prices.
- ✍ Industry is planning to invest Rs 45,000 Cr to build additional capacity of 100 mn tons. Government interference in price may hurt the sentiment to create the additional capacity and/ or the pace of expansion.

Conclusion:

- ✍ Not to increase cement price further for a year will not affect profitability much as feared in the market because we feel the current prices are roughly 5% to 7% lower than the landed cost if imported so there was scope to raise cement prices further by only 3-5percent whether industry announce price ceiling or not.
- ✍ Further current prices are ruling high around Rs 220 per bag which is 20 percent more as compared to previous year and we are in the month of March and as we all know from June onward when monsoon sets in the prices tends to go down for 3-4 months till Sept.
- ✍ The decision to freeze the prices has been taken very negatively by market players which we feel is more negative on sentiments nothing to do with the current fundamentals of cement stocks. So we shall come to know only after Sept, 2007 that how this price ceiling will affect the earnings of cement companies.
- ✍ At current prices of cement ruling around Rs 220 to Rs 240 per bag of 50 kg, we are of the opinion that this gives a very good margin of Rs 700 to Rs 800 per tons to Cement companies and with the market prices of cement stocks already gone down 25% to 35% from their peak level, make investments in these stocks attractive for a period of 4 to 6 months. **BUY**

J K Cem. (2nd Jan to 9th March 2007)Rain Comm. (2nd Jan to 9th March 2007)

Import prices of cement USD/Ton	Scenario		Remarks
	Before	After	
FOB	53.0	53.0	
Freight & Insurance	17.0	17.0	
CIF (US\$/ton)	70.0	70.0	
Rupee	45.0	45.0	
CIF (Rs/ton)	3,150.0	3,150.0	
Customs duty (%)	12.5	0.0	
Import duty (Rs/ton)	393.8	0.0	
CIF after duties (Rs/ton)	3,543.8	3,150.0	
CVD (Rs/ton)	408.0	618.0	
Cost after CVD (Rs/ton)	3,951.8	3,768.0	
Port handling charges	160.0	160.0	
Packing cost (Rs/ton)	120.0	120.0	
Landed cost (Rs/ton)	4,231.8	4,048.0	
Sales tax at 12.5%	529.0	506.0	
Price ex-port	4,760.7	4,554.0	
Inland freight	100.0	100.0	Only to the port city
Wholesale prices	4,860.7	4,654.0	
Dealer margin & Octroi	125.0	125.0	
Price/ton 4,985.7	4,779.0		
Price/bag	249.3	239.0	
All India average prices	221.0	221.0	
Discount	-11.3%	-7.5%	Even after price increase of Rs12/bag Indian cement will be cheaper by 7.5%

Source: Religare Research

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