

Gujarat Ambuja Cement

Building on strength

We raise our EPS estimates for 2007-08 by 19-22% owing to our higher volume and price estimates; improved margins due to blended cements; and the proposed merger of associate company ACEL. We maintain our Buy and raise our target price to Rs152.02.

Key forecasts

	FY04A	FY05A	FY06F	FY07F	FY08F
Revenue (Rsm)	19680.8	26034.8	58760.0	52956.1	58082.7
EBITDA (Rsm)	5380.8	7218.2	21180.6▲	21155.3▲	24158.1▲
Reported net profit (Rsm)	3378.4	4659.8	15316.5▲	14679.5▲	17011.1▲
Normalised net profit (Rsm) ¹	2948.2	4659.8	15316.5	14679.5	17011.1
Normalised EPS (Rs)	2.18	3.45	10.2▲	9.75▲	11.3▲
Dividend per share (Rs)	1.07	1.33	3.00▲	3.00▲	3.50▲
Dividend yield (%)	0.78	0.97	2.19	2.19	2.56
Normalised PE (x)	62.8	39.7	13.5▼	14.0▼	12.1▼
EV/EBITDA (x)	38.8	27.2	8.90	8.76	7.48
Price/book value (x)	7.76	7.25	5.67	4.41	3.52
ROIC (%)	6.59	9.55	34.7	30.9	29.0

1. Post-goodwill amortisation and pre-exceptional items
Source: Company data, ABN AMRO forecasts
Accounting Standard: Local GAAP

year to Jun, fully diluted

GAMB to drive volume growth through high blended cement sales

GAMB is in the process of setting up 2mmt grinding unit, and plans to ramp up the proportion of blended cements to total cement production from 45% to 70% by 2008. We believe this will improve margins from 36% in 2006F to 40% in 2007F. besides improving returns (33.4% to 41%) as incremental cement production is at a relatively low capital cost. GAMB's expansion project (a 2.3mmt clinker plant), which could potentially produce 3mmt of cement, is to go onstream by end-2008, raising its cement capacity by 17%.

GAMB continues to be the lowest-cost cement producer

GAMB's EBITDA/mt is one of the highest in the industry. In the July-September quarter, it was US\$25, followed by Grasim's US\$23. GAMB says it is investing aggressively in coal-based captive power across its plants. It is setting up a 60MW power plant in Gujarat, which it expects to be commissioned in 2007, and another 81MW of coal-based captive power across various other plants. We expect a 10% savings in per/kwh power cost on the commissioning of these units.

We have a positive industry outlook for the next two years

We maintain our positive view on the cement business in the medium term. We estimate an incremental cement capacity addition of 50mmt over FY06-09, with around 26mmt of capacity addition in 2008F itself. Assuming a gradual ramping up of these capacities, we forecast utilisation rates to remain at 95.3% in FY09, down marginally from 97% in FY07. Besides, our recent interaction with global cement machinery makers suggests scope for delays in deliveries, leading to a slippage of capacity addition from FY09 to FY10.

We raise our earnings estimates by 19-22%, target price to Rs152.02

We have revised our earnings estimates to give effect to: 1) a changeover to December year-end (making 2006 an 18-month period); 2) the proposed merger of its associate company ACEL with GAMB; and 3) our revised volume and cement price assumptions. Hence, we raise our DCF-based target price to Rs152.02.

Priced at close of business 13 November 2006. Use of ▲ ▼ indicates that the line item has changed by at least 5%.

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Buy

Absolute performance

n/a

Short term

Neutral

Market relative to region

Materials

India

Price

Rs136.90

Target price

Rs152.02 (from Rs102.47)

Market capitalisation

Rs206.15bn (US\$4.58bn)

Avg (12mth) daily turnover

Rs190.11m (US\$4.20m)

Reuters

GACM.BO

Bloomberg

GAMB IN

Asset allocation

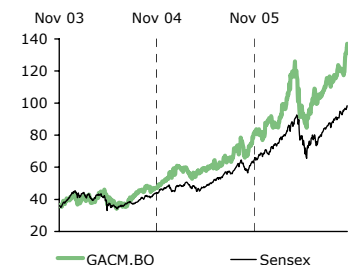
Equities Underweight

Cash Overweight

Bonds Overweight

Price performance (1M) (3M) (12M)

	1M	3M	12M
Price (Rs)	122.2	106.3	74.8
Absolute %	12.1	28.8	83.0
Rel market %	6.5	7.6	15.7
Rel sector %	7.4	17.3	47.0



Stock borrowing: Difficult

Volatility (30-day): 24.63%

Volatility (6-month trend): ↓

52-week range: 139.90-72.90

Sensex: 13399.00

BBG AP Construction: 275.86

Source: ABN AMRO, Bloomberg

Researched by

ABN AMRO Institutional
Equities Team

www.abnamrobroking.co.in

Table 1 : EPS revisions

	2006F	2007F	2008F
Old (Rs/share)	9	8	9.5
New (Rs/share)	10.17	9.75	11.30
Change (%)	13%	22%	19%

Note: The 2006 EPS numbers are now for an 18-month period ended 31/12/2006, as compared to our earlier estimate for 30/6/2006, reflecting the change to the company's year end. We also expect the merger of associate, ACEL to be achieved in 2006

Source: ABN AMRO forecasts

Table 2 : Key assumptions and sensitivity

	FY06F	FY07F	FY08F
Volume (mmt)	22	17	17.8
Average realisation (Rs/mt)	3031	3476	3624
EBITDA/mt (Rs)	963	1244	1357
1% change in cement price	3.1%	2.8%	2.7%
Sensitivity to EBITDA/mt			

Source: ABN AMRO forecasts

Table 3 : Gujarat Ambuja's future growth plans

Future growth plans	Commissioning
Projects	
60 MW power plant at Ambujanagar	
Phase 1	1Q07
Phase 11	2Q07
Expansion at Rabriyawas - 0.5mmt of clinker	June 2007
Grinding Stations: 2mmt	March 2007
2.3mmt clinkerisation plant at Chattisgarh	December 2008
Power plants of 81 MW at various locations	December 2008
Total capex over the next two years	Rs16bn

Source: Company data

Table 4 : July-Sept 2006 performance analysis of top five cement companies

Peer group quarterly performance	India				
	ACC	GAMB	Grasim	Ultratech	Cements
Sales volumes (mmt)	4.27	3.66	3.38	3.68	1.9
Sales Value (Rs m)	13916	11310	11412	10045	5163.5
EBITDA	3912	4256	3560	2664	1725.7
Margin (%)	28%	38%	31%	27%	33%
EBITDA/mt	916.2	1162.8	1053.3	723.9	908.3

Source: Company data, ABN AMRO

Table 5 : Trend in cement prices in GAMB's key markets (Rs/bag)

Trend in cement prices in key markets of GAMB (Rs/bag of cement)	Sep-06	Jun-06	Mar-06	Dec-05	Sep-05
Mumbai	217	214	193	172	171
Ahmedabad	193	188	167	155	152
Delhi	201	202	178	156	156
Jaipur	178	174	162	144	138
Kolkata	194	192	178	171	172

Source: Company data

Table 6 : Cement industry demand-supply forecasts (mmt)

Year-end March	Net effective Capacity #	Potential Supply at 95% utilisation	Domestic demand	Cement exports	Total Exports	Demand/ Supply
FY07F						
North	41.4	39.4	44.5			-5.2
East	13.0	12.4	20.8		0.7	-9.1
Central	31.4	29.9	10.4		1	18.5
North+East+Central	85.9	81.6	75.8		1.7	4.1
North+East+Central						0.0
West	27.4	26.0	28.8		8	-10.7
South	46.8	44.5	40.5			4.0
South+West	74.2	70.5	69.2		8	-6.7
Total All India	160.1	152.1	145.0	6.5	9.7	-2.6
Total Cement sales				151.48		
Total sales				154.68	9.6%	
Cement demand growth				10.1%		
Capacity utilisation rate				97%		
Capacity growth				5.1%		
FY08F						
North	49.9	47.4	49.0			-1.6
East	16.0	15.2	22.9		0.7	-8.4
Central	32.4	30.8	11.4		1	18.4
North+East+Central	98.4	93.5	83.3		1.7	8.4
North+East+Central						
West	28.9	27.5	31.6		5	-9.2
South	49.3	46.9	44.5			2.3
South+West	78.2	74.3	76.2		6	-7.8
Total All India	176.6	167.8	159.5	4.0	7.7	0.6
Total Cement sales				163.48	7.9%	
Total sales				167.18	8.1%	
Cement demand growth				7.9%		
Capacity utilisation rate				95%		
Capacity growth				10.3%		
FY09F						
North	59.4	52.2	53.4			-1.2
East	19.5	17.0	25.0		0.7	-8.7
Central	32.4	30.8	12.5		1	17.3
North+East+Central	111.4	100.0	90.8		1.7	7.4
North+East+Central						
West	28.9	27.5	34.5		5	-12.0
South	61.8	53.1	48.5			4.6
South+West	90.7	80.6	83.0		5	-7.4
Total All India	202.1	180.5	173.8	4.0	6.7	0.0
Total Cement sales				177.84		
Total sales				180.54		
Cement demand growth				8.8%		
Capacity utilisation rate				95.3%		
Capacity growth				14.4%		

Gross capacity would be 6.2mmt more, adding the non-operational capacity
Source: ABN AMRO, Cement Manufacturers Association

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GUJARAT AMBUJA CEMENT: KEY FINANCIAL DATA

Income statement

Rsm	FY04A	FY05A	FY06F	FY07F	FY08F
Revenue	19680.8	26034.8	58760.0	52956.1	58082.7
Cost of sales	-1069.2	-1244.0	-2492.6	-1993.1	-2160.7
Operating costs	-13231	-17573	-35087	-29808	-31764
EBITDA	5380.8	7218.2	21180.6	21155.3	24158.1
DDA & Impairment (ex gw)	-1686.1	-1954.1	-1971.3	-2185.5	-2274.5
EBITA	3694.7	5264.1	19209.3	18969.8	21883.7
Goodwill (amort/impaird)	n/a	n/a	n/a	n/a	n/a
EBIT	3694.7	5264.1	19209.3	18969.8	21883.7
Net interest	-784.3	-847.5	-800.0	-249.9	-174.6
Associates (pre-tax)	n/a	n/a	n/a	n/a	n/a
Forex gain / (loss)	n/a	n/a	n/a	n/a	n/a
Exceptionals (pre-tax)	n/a	n/a	n/a	n/a	n/a
Other pre-tax items	504.9	745.7	500.0	100.0	100.0
Reported PTP	3415.3	5162.3	18909.3	18819.9	21809.1
Taxation	-467.1	-502.5	-3592.8	-4140.4	-4798.0
Minority interests	n/a	n/a	n/a	n/a	n/a
Exceptionals (post-tax)	430.2	0.00	0.00	0.00	0.00
Other post-tax items	0.00	0.00	0.00	0.00	0.00
Reported net profit	3378.4	4659.8	15316.5	14679.5	17011.1
Normalised Items Excl. GW	430.2	0.00	0.00	0.00	0.00
Normalised net profit	2948.2	4659.8	15316.5	14679.5	17011.1

Source: Company data, ABN AMRO forecasts

year to Jun

Balance sheet

Rsm	FY04A	FY05A	FY06F	FY07F	FY08F
Cash & market secs (1)	688.3	865.3	1953.0	1874.3	2055.8
Other current assets	4226.5	5013.1	9573.9	9710.7	11443.1
Tangible fixed assets	24982.2	23633.4	27581.1	33845.9	40199.7
Intang assets (incl gw)	n/a	n/a	n/a	n/a	n/a
Oth non-curr assets	10109.7	11250.6	11250.6	13250.6	16250.6
Total assets	40006.7	40762.4	50358.6	58681.4	69949.1
Short term debt (2)	6199.0	5781.2	1211.1	0.00	0.00
Trade & oth current liab	3474.1	3957.5	8532.0	7689.3	8433.6
Long term debt (3)	6497.8	5493.3	4286.5	4193.3	2976.1
Oth non-current liab	0.00	0.00	0.00	0.00	0.00
Total liabilities	16170.9	15232.0	14029.6	11882.6	11409.8
Total equity (incl min)	23835.8	25530.1	36329.0	46798.8	58539.3
Total liab & sh equity	40006.7	40762.1	50358.6	58681.4	69949.1
Net debt (2+3-1)	12008.5	10409.2	3544.6	2319.0	920.4

Source: Company data, ABN AMRO forecasts

year ended Jun

Cash flow statement

Rsm	FY04A	FY05A	FY06F	FY07F	FY08F
EBITDA	5380.8	7218.2	21180.6	21155.3	24158.1
Change in working capital	4534.4	-303.2	13.7	-979.5	-988.0
Net interest (pd) / rec	-784.3	-847.5	-800.0	-249.9	-174.6
Taxes paid	-467.1	-502.5	-3592.8	-4140.4	-4798.0
Other oper cash items	504.9	745.7	500.0	100.0	100.0
Cash flow from ops (1)	9168.7	6310.7	17301.5	15885.5	18297.5
Capex (2)	-7583.7	-449.1	-5919.0	-7000.0	-7000.0
Disposals/(acquisitions)	0.00	0.00	0.00	0.00	0.00
Other investing cash flow	907.4	-1140.9	0.00	-2000.0	-3000.0
Cash flow from invest (3)	-6676.3	-1590.0	-5919.0	-9000.0	-10000
Incr / (decr) in equity	4592.3	-912.3	0.00	308.0	0.00
Incr / (decr) in debt	-4816.0	-1422.3	-5776.9	-1304.2	-1217.2
Ordinary dividend paid	-1420.7	-1891.6	-4517.6	-4517.6	-5270.6
Preferred dividends (4)	n/a	n/a	n/a	n/a	n/a
Other financing cash flow	n/a	n/a	n/a	n/a	n/a
Cash flow from fin (5)	-1644.4	-4226.2	-10295	-5513.9	-6487.8
Forex & disc ops (6)	-468.5	-317.5	-0.30	-1450.3	-1628.3
Inc/(decr) cash (1+3+5+6)	379.5	177.0	1087.7	-78.6	181.5
Equity FCF (1+2+4)	1585.0	5861.6	11382.5	8885.5	11297.5

Lines in bold can be derived from the immediately preceding lines.

Source: Company data, ABN AMRO forecasts

year to Jun

GUJARAT AMBUJA CEMENT: PERFORMANCE AND VALUATION

Standard ratios	Gujarat Ambuja					Associated Cement			Holcim		
Performance	FY04A	FY05A	FY06F	FY07F	FY08F	FY06F	FY07F	FY08F	FY06F	FY07F	FY08F
Sales growth (%)	13.5	32.3	125.7	-9.88	9.68	80.1	12.9	8.74	17.1	6.74	3.69
EBITDA growth (%)	12.9	34.1	193.4	-0.12	14.2	218.9	20.7	14.0	12.0	5.41	3.54
EBIT growth (%)	21.2	42.5	264.9	-1.25	15.4	303.4	19.7	12.4	13.7	5.04	3.55
Normalised EPS growth (%)	14.6	58.1	195.1	-4.16	15.9	215.8	20.8	15.4	16.7	3.87	8.01
EBITDA margin (%)	27.3	27.7	36.0	39.9	41.6	28.7	30.6	32.1	24.0	23.7	23.6
EBIT margin (%)	18.8	20.2	32.7	35.8	37.7	24.8	26.3	27.1	17.4	17.2	17.1
Net profit margin (%)	15.0	17.9	26.1	27.7	29.3	18.1	19.5	20.7	8.41	8.19	8.54
Return on avg assets (%)	8.71	12.9	34.8	27.2	26.6	20.4	21.1	21.6	6.87	7.02	7.19
Return on avg equity (%)	13.7	18.9	49.5	35.3	32.3	39.9	35.5	32.0	14.9	14.0	13.8
ROIC (%)	6.59	9.55	34.7	30.9	29.0	26.5	25.8	26.9	9.46	9.79	10.2
ROIC - WACC (%)	-4.91	-1.95	23.2	19.4	17.5	15.9	15.2	16.3	3.66	3.95	4.31
				<i>year to Jun</i>			<i>year to Dec</i>			<i>year to Dec</i>	
Valuation											
EV/sales (x)	10.6	7.55	3.21	3.50	3.11	3.43	2.94	2.67	2.01	1.89	1.78
EV/EBITDA (x)	38.8	27.2	8.90	8.76	7.48	12.0	9.59	8.31	8.24	7.85	7.40
EV/EBITDA @ tgt price (x)	43.1	30.4	9.97	9.84	8.43	12.8	10.3	8.89	8.68	8.26	7.79
EV/EBIT (x)	56.6	37.3	9.81	9.77	8.26	13.9	11.2	9.83	11.2	10.7	10.1
EV/invested capital (x)	5.83	5.47	4.73	3.77	3.04	4.60	4.12	3.45	1.54	1.53	1.49
Price/book value (x)	7.76	7.25	5.67	4.41	3.52	6.16	4.69	3.73	2.06	1.87	1.70
Equity FCF yield (%)	0.86	3.17	5.52	4.31	5.48	3.49	7.41	3.36	4.58	6.16	6.72
Normalised PE (x)	62.8	39.7	13.5	14.0	12.1	18.1	15.0	13.0	14.3	13.7	12.7
Norm PE @tgt price (x)	69.7	44.1	14.9	15.6	13.5	19.4	16.0	13.9	15.6	15.0	13.9
Dividend yield (%)	0.78	0.97	2.19	2.19	2.56	1.18	1.57	1.96	1.77	1.95	2.27
				<i>year to Jun</i>			<i>year to Dec</i>			<i>year to Dec</i>	
Per share data	FY04A	FY05A	FY06F	FY07F	FY08F	Solvency	FY04A	FY05A	FY06F	FY07F	FY08F
Tot adj dil sh, ave (m)	1351.9	1351.9	1505.9	1505.9	1505.9	Net debt to equity (%)	50.4	40.8	9.76	4.96	1.57
Reported EPS (INR)	2.50	3.45	10.2	9.75	11.3	Net debt to tot ass (%)	30.0	25.5	7.04	3.95	1.32
Normalised EPS (INR)	2.18	3.45	10.2	9.75	11.3	Net debt to EBITDA	2.23	1.44	0.17	0.11	0.04
Dividend per share (INR)	1.07	1.33	3.00	3.00	3.50	Current ratio (x)	0.51	0.60	1.18	1.51	1.60
Equity FCF per share (INR)	1.17	4.34	7.56	5.90	7.50	Operating CF int cov (x)	13.3	9.04	27.1	81.1	133.3
Book value per sh (INR)	17.6	18.9	24.1	31.1	38.9	Dividend cover (x)	2.08	2.46	3.39	3.25	3.23
				<i>year to Jun</i>						<i>year to Jun</i>	

Priced as follows: GACM.BO - Rs136.90; ACC.BO - Rs1019.45; HOLZ.VX - SFr110.10
Source: Company data, ABN AMRO forecasts

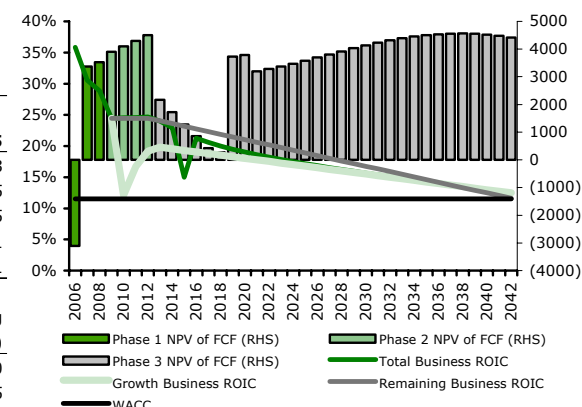
GUJARAT AMBUJA CEMENT: VALUATION METHODOLOGY

Economic Profit Valuation			Rs m	%	Discounted Cash Flow Valuation			Rs m	%			
Adjusted Opening Invested Capital			46293.9	22	Value of Phase 1: Explicit (2006 to 2008)			3783.6	3			
NPV of Economic Profit During Explicit Period			11453.3	5	Value of Phase 2: Value Driver (2009 to 2012)			16808.0	12			
NPV of Econ Profit of Remaining Business (1, 2)			46424.3	22	Value of Phase 3: Fade (2013 to 2042.24)			117023.3	85			
NPV of Econ Profit of Net Inv (Grth Business) (1, 3)			108248.8	51	Terminal Value			0.0	0			
Enterprise Value			212420.3	100	Enterprise Value			137614.9	100			
Plus: Other Assets			16500.0	8	FCF Grth Rate at end of Phs 1 implied by DCF Valuation			9.6				
Less: Minorities			0.0	0	FCF Grth Rate at end of Phs 1 implied by Current Price			34.9				
Less: Net Debt (as at 13 Nov 2006)			0.0	0								
Equity Value			228920.3	108								
No. Shares (millions)			1505.9									
Per Share Equity Value (Rs)			152.02									
Current Share Price (Rs)			136.90									
Sensitivity Table												
		No of Years in Fade Period										
		15	18	20	23	25						
WACC	9.5%	163.84	184.65	198.91	220.96	236.13						
	10.5%	131.28	145.26	154.72	169.16	178.95						
	11.5%	107.16	116.58	122.90	132.44	138.85						
	12.5%	89.01	95.35	99.60	105.97	110.21						
	13.5%	75.16	79.42	82.28	86.57	89.41						
Performance Summary						Phase 2 Avg (2009 - 2012)						
		2006	2007	2008								
Invested Capital Growth (%)		13.6	21.9	20.6	16.0							
Operating Margin (%)		36.0	39.9	41.6	36.5							
Capital Turnover (x)		0.7	1.4	1.0	1.0							

Source: ABN AMRO estimates

- In periods following the Explicit Period i.e. Phase 2 and Phase 3
- Remaining Business is defined as Capital as at the end of Phase 1 and capex = depreciation thereafter
- Net Investment is defined as capex over and above depreciation after Phase 1

Returns, WACC and NPV of Free Cash Flow



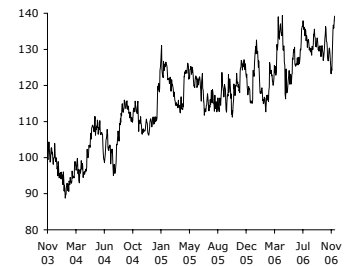
Gujarat Ambuja Cement

Company description

GACL, which was set up in 1986 with a capacity of 0.7mmt, has now grown to become a 16mmt cement company spread across five plants located in northern, western and eastern India. GACL has been one of the most innovative cement companies in India, as it uses sea transportation to move cement in India, besides, operating three terminals, seven dry bulk ships and a captive jetty in the state of Gujarat. It has also runs 250MW of captive power plants across its various cement plants, which gives it access to a cheaper and more reliable source of power. Recently, Holcim has acquired a stake in the company from the promoter family, and currently Holcim holds around 22% of the company. GACL has successfully acquired companies like Modi Cement and DLF Cements in the past 10 years, and has made them extremely profitable, and later merged them with itself.

Buy

Price relative to country



Strategic analysis

Average SWOT company score: 3

Sales composition, by state

Strengths

GACL has been one of most innovative cement companies in India in terms of managing logistics and production costs. Therefore it has been able to sustain above-industry average EBIDTA margins. Holcim's entry into Ambuja management should further improve GACL's innovation.

4

Weaknesses

GACL has relatively lopsided exposure to the northern and western markets, which makes it vulnerable to price fluctuations in these areas. The recent merger of Ambuja Cement Eastern should broaden its geographical presence.

2

Opportunities

GACL could look at strategic acquisitions in key markets to drive further growth, given its excellent track record in turning around acquired cement companies.

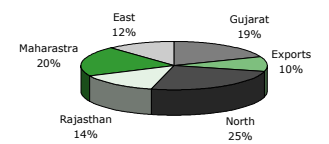
3

Threats

Any significant slowdown in the export market could impact pricing in the state of Gujarat, as a major portion of the surplus in that state is exported.

2

Scoring range is 1-5 (high score is good)



Source: Company

Market data

Headquarters

P.O Ambuja Nagar, Taluka Kodinar, Dist. Junagadh, Gujarat-362715

Website

www.gujaratambuja.com

Shares in issue

1505.9m

Freefloat

65%

Majority shareholders

FIIS (32%), Holcim (23%), Founder Promoters (8%)

India

Country view

Neutral

Country rel to Asia Pacific

The market looks expensive, but we believe it will remain supportive when regional funds seek a domestically-driven home with continuing robust earnings growth. The ABN AMRO Indian PMI suggests the economy is still powering ahead despite the global headwinds, thanks to its domestically-oriented economic structure. At the sector level, we still like autos, software and construction-related stocks.

The country view is set in consultation with the relevant company analyst but is the ultimate responsibility of the Strategy Team.



Competitive position

Average competitive score: 3-

Broker recommendations

Supplier power

Given GACL's scale of operations, it enjoys reasonable scale to swing better terms of trade with suppliers of raw materials and freight operators.

3-

Barriers to entry

Cement is a commodity business and has no entry barrier. GACL has a strong equity in the retail market, which helps it to sell a higher proportion of its sales to a lucrative retail market.

3-

Customer power

GACL's brand equity is strong in the retail market and it commands a price premium of 3-4% for its cement compared with smaller players.

3-

Substitute products

There is no substitute for cement in civil construction. There exist threats from imports in coastal locations like Gujarat and Maharashtra, but given India's port infrastructure the threat is limited.

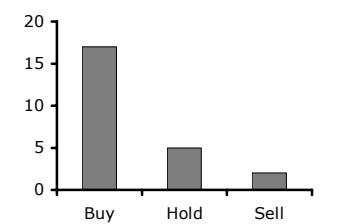
3-

Rivalry

The top end of the Indian cement industry is well consolidated with five players accounting for 60%, but there are 40+ small players that could lead to price competition in many markets.

3-

Scoring range 1-5 (high score is good) Plus = getting better Minus = getting worse



Source: Bloomberg