



Q1FY2008 Cement earnings preview

Cement prices on the rise

- ◆ The growth in cement volumes is expected to have been subdued in Q1FY2008 with capacity utilisations touching 100% and no major capacity having come up in the period. Amongst the front-line stocks, ACC is expected to report a volume growth of 14% year on year (yoy) and of 9% quarter on quarter (qoq) for Q1FY2008, thanks to the incremental volumes from the addition of 0.9 million metric tonne (MMT) capacity at its Lakheri unit. Grasim Industries is expected to report an 8.2% growth yoy for the quarter. Amongst our mid-cap companies, Shree Cement is likely to report a huge volume growth of 23% on account of its capacity expansion at Ras. We expect the Sharekhan cement universe to report a combined volume growth of 7.1%.
- ◆ Cement prices across the country remained more or less stable throughout the quarter under review except in the south. In the south, Andhra Pradesh witnessed a hike of Rs5-9 per bag in the first week of June whereas Tamil Nadu saw price hikes of Rs6-7 per bag in May and of Rs7-8 per bag in June. Thus except for the south-based companies, the cement realisation of the cement industry is expected to be more or less flat on a sequential basis for Q1FY2008.
- ◆ Amongst our front-line cement stocks, we expect ACC to report a top line growth of 24% yoy to Rs1,820 crore on the back of a higher volume growth. We expect Grasim Industries to report a top line growth of 28.6% to Rs2,414 crore backed by firm viscose staple fibre (VSF) prices. We expect Shree Cement to report a top line growth of 34% yoy to Rs413 crore.
- ◆ On the earnings front, we expect our cement universe to clock a growth of 39% yoy backed by an 85% growth in Orient Paper and Industries and a 48% growth in Grasim Industries on account of higher cement realisations and firm VSF prices. On account of the merger of Visaka Cement and India Cements, we expect India Cements' profit to touch Rs200 crore.
- ◆ Contrary to the industry's expectations, the cement price freeze will no longer be applicable as clarified by the finance minister recently. We thus expect the demand-supply economics to govern the cement pricing and any cost increase to be passed on to the consumer, as witnessed in Andhra Pradesh recently. We have already seen that prices have increased by Rs3-5 per bag across the country in first week of July. Prices in Andhra Pradesh and Tamil Nadu have already risen by Rs5-15 per bag. With the industry utilisation levels reaching 100%, we believe the higher realisations augur well for the cement players, as the same would result in better than expected profitability even though the volume growth will remain subdued going ahead. We rate Grasim Industries and Jaiprakash Associates as our top picks in the sector as their non-cement businesses are expected to do extremely well going ahead. Amongst our mid-cap universe, we like Orient Paper and Industries, as it trades at a cheap valuation of USD23 on its expanded capacity.

Quarterly estimates

(Rs crore)	Net sales			Profit after tax		
	Q1FY08E	Q1FY07	% change	Q1FY08E	Q1FY07	% change
Shree Cement	422.7	309.4	36.6	113.9	90.4	26
JK Cement	323.5	279.5	15.7	46.9	33.0	42
ACC	1820.1	1462.0	24.0	368.9	259.1	42
UltraTech	1335.3	1180.3	13.1	233.0	210.8	11
India Cements*	705.6	485.2	45.4	199.4	112.7	77
Madras Cement	446.0	340.9	30.8	93.6	78.9	19
Grasim	2450.1	1877.0	30.5	462.3	311.9	48
Orient Paper	147.7	141.6	4.3	48.2	26.0	85

*We have assumed merger of Visaka Cement, consequently the numbers are not comparable.

Shree Cement to witness highest volume growth; south-based companies enjoy higher prices

With the industry's capacity utilisation levels rising to almost 100% during the quarter, volume growth was broadly muted during the period. For the months of April and May, the southern region witnessed the highest dispatch growth of 13% yoy, thanks to the strong demand.

Amongst the companies in our universe, Shree Cement will witness the highest volume growth on account of its additional 1.5MMT facility at Ras whereas ACC will witness a volume growth of 14% with the additional volumes kicking in from its Lakheri unit. JK Cement will witness a decline of 1% in its volumes as it carried out a shutdown and maintenance exercise in the months of April and May. We expect our universe of stocks to witness a volume growth of 7.1% yoy.

Dispatches for Q1FY2008

Particulars	Q1FY08E	Q1FY07	% yoy
Shree Cement	1.41	1.12	25.4
JK Cement	0.91	0.93	-1.1
ACC	5.30	4.60	14.0
UltraTech	4.58	4.45	3.0
India Cements	2.30	2.00	6.5
Madras Cement*	1.42	1.28	10.8
Grasim	3.87	3.60	8.2
Orient Paper*	0.57	0.58	-1.6
Total	25.20	23.60	7.1

*We have assumed the volumes for June

Source: Sharekhan

South-based companies to benefit from higher prices

As mentioned in our earlier updates, cement prices across the country remained stable in the quarter except in the southern region (mainly Andhra Pradesh and Tamil Nadu), which saw significant price hikes. The price in Tamil Nadu increased by Rs6-7 per bag in May and by Rs7-8 per bag in June. Prices in Andhra Pradesh were hiked by Rs5-9 per bag in June to pass on the hike in the coal royalty. Thus on a sequential basis, we expect our south-based companies, namely India Cements and Madras Cement, to witness a realisation growth of 11% and 6% respectively.

On a year-on-year basis too, we expect our south-based companies to clock the highest realisation growth. JK Cement will also witness a high realisation growth of 17%, thanks to the increased sales of white cement, which commands higher realisations.

Cost to remain stable in the quarter

We expect the costs to remain stable in the quarter with a few exceptions. The rising international coal prices will affect India Cements and Madras Cement which together consume close to 50-60% of the country's coal imports. JK

Cement will witness an additional expenditure of Rs2 crore spent towards maintenance and shutdown. The increase in the coal royalty will not have any impact on the cement companies, as mentioned in our earlier report.

Per tonne analysis

Particulars	Realisations			EBITDA per tonne		
	Q1 FY08	Q1 FY07	yoy (%)	Q1 FY08	Q1 FY07	yoy (%)
Shree Cement	2997.8	2752.5	9	1236.0	1223.1	1.1
JK Cement	3532.4	3018.4	17	949.8	709.5	33.9
ACC	3434.2	3157.7	9	1047.6	983.9	6.5
UltraTech	2914.8	2652.4	10	896.7	841.8	6.5
India Cements	3068.0	2482.9	24	1092.0	847.6	28.8
Madras Cements	3145.0	2663.2	18	1068.0	1065.4	0.2
Orient Paper*	2597.0	2449.83	6	1168.7	821.8	42.0

*EBIT per tonne

We expect our universe to clock a 39% earnings growth yoy

We expect Orient Paper and Industries to witness the highest earnings growth of 85% on account of its efficient cost control measures (coupled with a lower base). We expect Grasim Industries to witness a growth of 48% yoy on the back of higher cement realisations and firm VSF prices.

We believe that UltraTech Cement will be a laggard in our universe with an earnings growth of only 11%.

India Cements will witness a huge jump in its profits with the consolidation of Visaka Cement, which has exposure to lucrative markets and accumulated losses sitting on its books that would lead to tax benefits.

Outlook

Contrary to the industry's expectations, the cement price freeze will no longer be applicable as clarified by the finance minister recently. We thus expect the demand-supply economics to govern the cement pricing and any cost increase to be passed on to the consumer, as witnessed in Andhra Pradesh recently. We have already seen that prices have increased by Rs3-5 per bag across the country in first week of July. Prices in Andhra Pradesh and Tamil Nadu have already risen by Rs5-15 per bag.

With the industry utilisation levels reaching 100%, we believe the higher realisations augur well for the cement players, as the same would result in better than expected profitability even though the volume growth would remain subdued going ahead. We rate Grasim Industries and Jaiprakash Associates as our top picks in the sector as their non-cement businesses are expected to do extremely well going ahead. Amongst our mid-cap universe, we like Orient Paper and Industries, as it trades at a cheap valuation of USD23 on its expanded capacity.

Valuation table

	Price target	PER		EV/EBITDA		EV/Ton	
		FY08E	FY09E	FY08E	FY09E	FY08E	FY09E
ACC	880.0	14.6	15.8	9.5	9.9	213.6	200.0
Grasim	3350.0	12.5	10.5	6.2	4.8	-	-
UltraTech	935.0	12.5	11.7	6.7	5.9	171.4	135.8
Shree Cement	1500.0	10.7	9.8	6.1	5.0	141.5	104.6
JK Cement	200.0	4.8	5.7	3.6	4.6	78.9	60.8
Madras Cements	3500.0	10.6	9.2	7.6	5.2	130.1	100.6
India Cement	231.0	9.2	9.6	6.1	5.3	141.2	111.6
Jaiprakash Associates	850.0	20.8	14.5	13.4	8.3	-	-
Orient Paper	680.0	4.5	4.6	2.7	3.1	52.0	46.0

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

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