



Cement Sector Update

Feb 2019

Research Analyst

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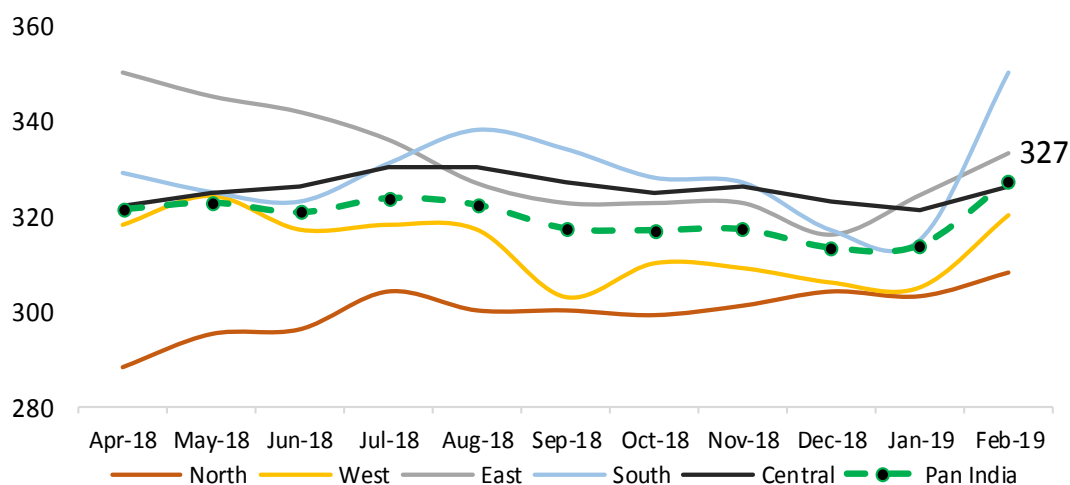
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Sector Overview

The cement industry has been undergoing a turbulent period of weak pricing and high input cost for the whole 9mFY19. High Volume sales were the only bright spot for the industry in this period. As of Jan 2019, total cement production in India have totaled 272MT and is expected to reach 330MT by the end of FY19. According to industry, overall cement demand is expected to grow at a CAGR of 7-8% for the next 2-3 years.

Also after a long drought, cement makers across India have increased prices in February 2019 by as much as INR13-17 per bag across the country. While Southern region witnessed the steepest hike of INR30-40 per bag followed by INR15-20 per bag hike in the West and INR12-15 per bag hike in the East, prices in North and Central region remained flattish during the month of Feb. To sweeten it further, Power & Fuel cost and Diesel cost have also softened by around 20% from their recent high in Q2FY19. This would further improve the margins for the whole cement industry. However, it is too early to call if the pricing power has returned in the industry since due to upcoming general elections the demand may remain muted for the next two quarters which could eventually put pressure on the recently hiked prices.

Cement Price trend per bag



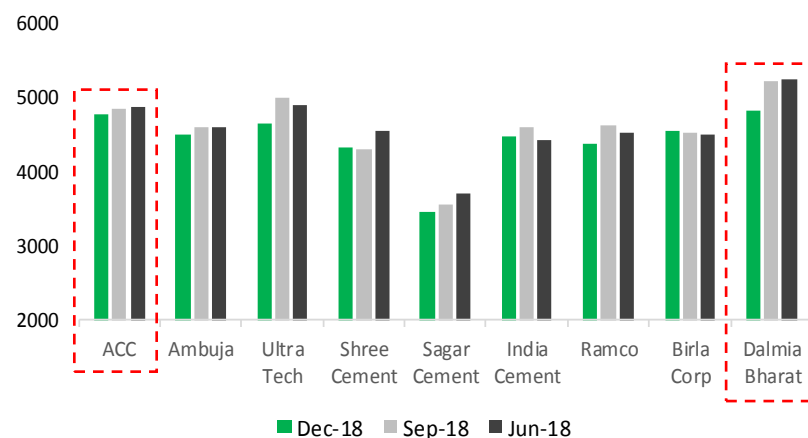
Source: SMIFS Research

- In FY19 overall **pan India average cement prices till Feb 2019 were down by around 3% to INR327 per bag** compared to FY18.
- The average cement prices in the North in FY19 till Feb 2019 is INR298, which is flattish compared to FY18 average cement prices in that region. Total cement market size in the North is around 85-90MTPA commanding a **average capacity utilisation of 80-85%.**
- In the same period average prices in the East were INR334 per bag, down by 4% compared to FY18, South average prices were also down by 5-6% to INR329 per bag, West average prices were down by 1% compared to FY18 to INR312 per bag and Central average prices were INR325 per bag, flattish compared to FY18.

9 months ended FY19 performance comparison

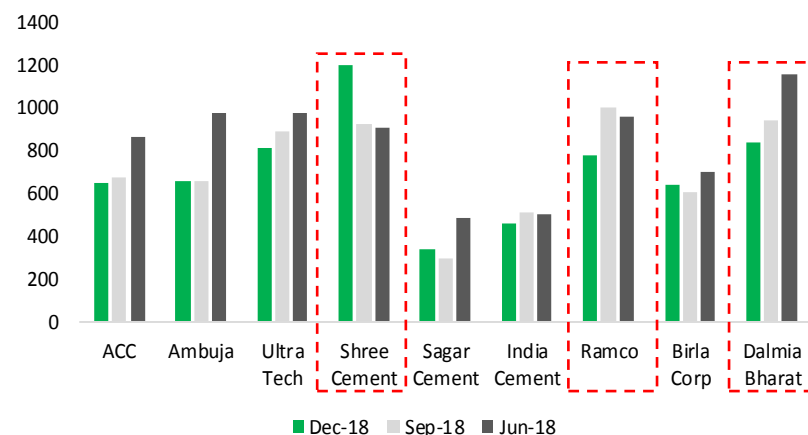
For the 9mFY19, cement industry has seen high YoY volume growth on the back of strong demand from Infra, low cost housing and rural housing. However, the profitability has dipped in this period mainly due to weak realization and high input cost. Here's how the 9mFY19 period was like for the cement industry.

Realisation Per ton



ACC, Dalmia Cement and Ultratech have achieved a higher realization than the industry average. The average realization for the Top 5 cement players in the industry were about INR4619 per ton.

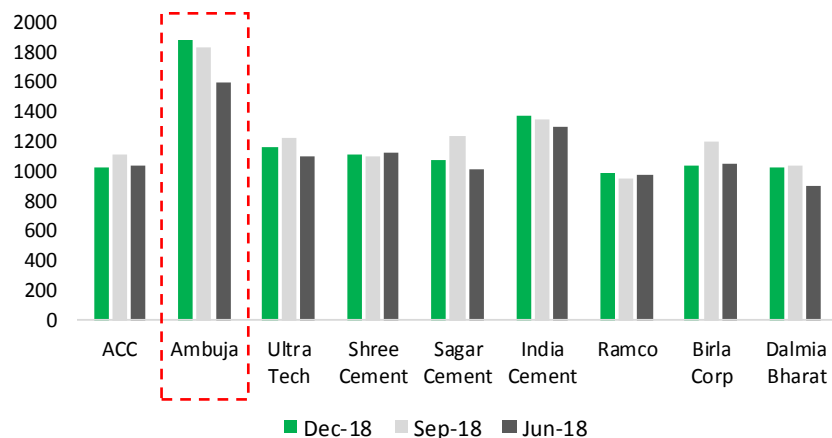
EBITDA per ton



Shree Cement, Ramco and Dalmia cements were the most cost effective in 9mFY19. Whereas, India Cements, Birla Corp and Sagar Cement clocked a lower EBITDA/ton. The average EBITDA/ton of these 3 players were down by around 65-70% from the top 5 cement players in the industry.

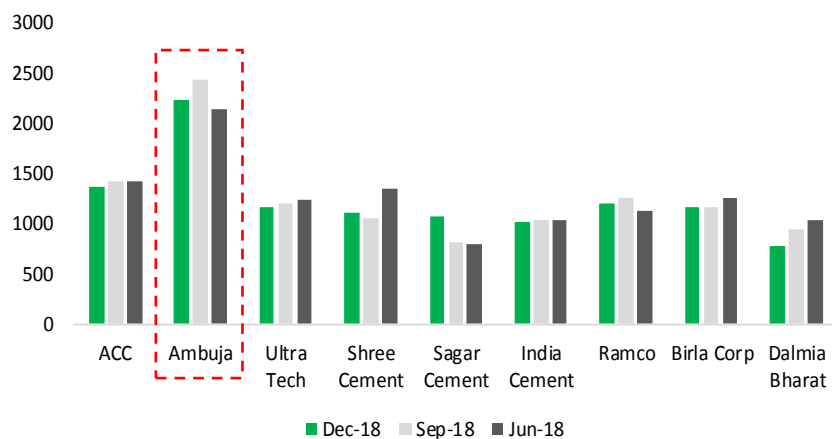
Source: Company Data, SMIFS Research

Power & Fuel cost per ton



Power & fuel cost per ton has reduced profit margins for all Cement players. **Ambuja cement** witnessed a sharp hike in Power cost. Whereas, Ramco Cements witnessed a lower Power & Fuel cost per ton.

Freight & Forwarding cost per ton



Freight cost has been on a steep rise due to high diesel price and high insurance cost till H1FY19. **Ambuja cement** have witnessed a higher than industry average freight cost per ton. Whereas Dalmia Cements has proved to be most cost efficient in terms of Freight & Forwarding expense per ton.

Clinker capacity Addition by FY21 Region-wise break up						(In MT)
S.I	Name	South	East	Central	West	North
1	Ultratech Cement					2.3*
2	ACC			3		
3	Ambuja					3.1
4	Dalmia Bharat		3			
5	Shree Cement					
6	Ramco	4.7				
7	Birla Corp				3.9	
8	Orient Cement	3				
9	Chettinand Cement	2.1				
10	Nuvoco					
11	JSW cement					
12	Penna Cement	2				
13	Wonder Cement					2
14	Others					
Total		11.8	3.0	3.0	3.9	5.1

* chances of being scrapped

Particulars	FY17	FY18	FY21E
Installed Cement capacity	440	455	520
Intalled Clinker capacity	310	320	350
Cement production	280	297	392
Clinker production	212	220	280
Cement Utilisation (%)	64%	65%	75%
Clinker Utilisation (%)	68%	69%	80%
CC ratio	1.32	1.35	1.40

Source: Company Data, SMIFS Research

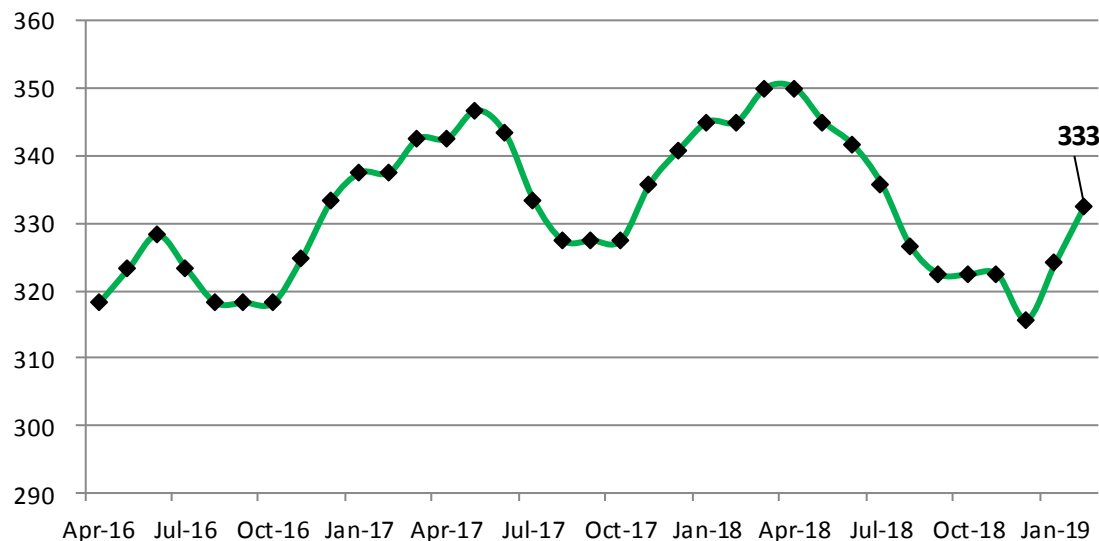
Cement Capacity(MT) addition					FY21E
Name	South	East	Central	West	North
Ultratech	-	-	-	-	-
ACC	-	1.1	4.8	-	-
Ambuja	-	-	-	-	1.8
Dalmia Bharat	3.0	8.9	-	-	-
Shree Cement	3.0	5.5	-	2.0	-
Birla Corp	-	-	1.2	3.9	-
Ramco	4.1	2.1	-	-	-
J.K lakshmi	-	-	-	-	-
J.K Cement	-	-	-	-	-
Rest	6.8	7.9	5.7	1.0	-
Total	16.9	25.5	11.7	6.9	1.8

- We expect capacity addition of 60-65MT by FY21 by almost all the cement majors and total Cement capacity to reach 520MT.
- Among the regions, East would witness the highest addition, an increase in capacity to the extent 25-27MT; followed by South where capacity close to 17MT could be added.
- However most of the addition is coming in the grinding capacity. Clinker capacity addition is limited to the extent of 25-30MT. Hence, clinker utilisation to remain significantly higher than cement utilisation levels.
- As on FY18 current clinker capacity in India is around 320MT. By FY21 clinker capacity would increase to 345-350MT.
- Assuming Cement to clinker ratio of 1.4 and clinker utilisation of 80% we can expect that max increase in cement supply would be in the range of 390 -400MT. This would mean overall cement utilisation would be around 75%.

Into the streets

We recently conducted our monthly channel checks on cement prices in the Eastern market. Here's what the picture looks like on the ground level market.

Cement Prices in East



Source: SMIFS Research

*wholesale prices including GST

- In months of January and February the cement price increased by INR15-18 per bag or 6% over Dec'18 prices.
- Current Feb exit prices have gone up to INR333 per per bag.
- Comparing YoY basis in the months of Jan and Feb, cement prices were down by INR10 per bag or 3.2%.
- The scenario is pretty same even during the 11 month period FY19, price in this period fell by INR16 per bag or around 5% over March'18 prices. Whereas last year in the same period the prices were slightly down by INR5 per bag.
- The increased prices were not well accepted among the cement dealers. The volume uptick have been rather weak in the last two months which is typically a good period in the cement industry.
- Current Freight cost typical for cement transportation is similar to Dec'18 rates i.e. at INR14-16 per ton-km.
- There is a fairly healthy demand coming from the road construction and rural housing.

Industry overview

- India's GDP is expected to grow at 7-7.4% in FY19 and FY20. It can be assumed that cement demand in India to grow at 1.0x to GDP growth rate.
- As per the management the outlook for growth in cement sector to remain strong on the back of steady demand from Rural housing, Infra projects and Low cost housing. The management expects the cement demand to grow at a CAGR of 7-8% over the next 2-3 years.
- For constructing standard 1km concrete road around 2500 tons of cement is required.
- In the month of February 2019, price hike of INR30-40 per bag is taken in South, INR5-7 per bag hike taken in the East, INR5 per bag taken in West and in the North slight price hike was taken but was rolled back eventually.
- Prices of imported petcoke have come down from earlier USD110-13 during Q3FY19 and is currently hovering around USD98-100 per ton.

SHREE CEMENT LIMITED

CMP (INR) : 17527	TTM P/E(x) : 44.11	P/B(x) : 6.85
Market Cap (INR Cr.) : 61061	FV (INR) : 10.00	52 Week High/Low : 19260/13125

Key Takeaways:

- Current clinker capacity of Shree Cement is around 23 MMT (East-5.2 MMT, North-17.8 MMT) and grinding capacity of around 39 MMT (excluding the upcoming grinding units in Odisha, Jharkhand and Pune).
- The project work for Grinding units in Jharkhand (2.5MT) and Odisha (3 MT) is expected to be completed by June 2019 and Sept 2019 respectively. Both the plants are expected to get commissioned by Dec 2019.
- Total capex guidance for FY19 is INR1700 crore and INR1200 crore for FY20.
- As per the Shree cement management, Ultratech could scrap its expansion of 3.5MT Integrated Unit in the North. The total clinker addition in the North as of now is being put up by Wonder cements (2MT) and Ambuja (3.1MT). Hence, the incremental cement supply would be limited to the extent clinker addition in the region.***
- For the company cost of coal based power comes to INR3.5 per unit whereas cost of WHRS (Waste Heat Recovery System) based power comes to INR0.3 per unit which is just the O&M expense. As per the management, to produce 1MT of Cement 0.4-0.6kg of coal is required.

- The company has launched a premium brand “Roofon” which is INR20-40 per bag higher than its current normal brand. However, this product will take another 1 year to get established in the market.
- The company has started focusing more on improving realisations and hence, the Trade to Non-Trade mix has come down to 70-30 from earlier 60-40. This would improve the EBITDA margin of the company. Currently, Shree cement has EBITDA per ton of around INR1200 which is above the industry average.
- ***For the company its clinker capacity in the North is running at 90% capacity. The Industry average is also at the similar levels in North.***
- In the trade market, the company’s brand comes under Category B, whereas Category A includes brands of Ultratech, ACC and Ambuja. There is price difference of INR20-40 per bag between category A and B.
- Current fuel mix for the company is 60% petcoke and 40% Imported coal. The company imports 100% of its coal requirement from Saudi Arabia and USA. Imported coal contains higher calorific value than domestic coal and generates more heat. Current price of Imported coal is hovering around USD100 per ton.
- The company does not procure any coal requirement from Coal India as there is no certainty in supply and also because of low calorific value in the domestic coal.
- ***Due to slight ease off in the diesel price the management expects some savings to accrue in freight cost in the Q4FY19.***
- ***The company has recently won mining lease at Chhattisgarh, Gujarat and Rajasthan. All of which having capacity above 150MT and a life of more than 50 years. Moreover, the company’s existing limestone reserves have a residual life of around 40 years.***
- As per the management, the production of Union Cement (UAE) have been ramped up to 13000 tons per day and looks to export 70% of production. Currently, this subsidiary is facing some headwinds as the trade relation has deteriorated between UAE and other Mid-East countries. The company is currently earning an EBITDA of 6-7 mn UAE Dirham.

Current and upcoming Plant capacity

Plants	Type	Region	Clinker (MT)	Cement (MT)	Thermal Power (MW)	WHRS (MW)	Wind Power (MW)
Beawar	IU	Rajasthan	3.0	3.6	344.0	21.0	-
Ras	IU	Rajasthan	12.4	7.0	136.0	75.0	-
Jobner	GU	Rajasthan	-	1.5	-	-	-
Suratgarh	GU	Rajasthan	-	1.8	-	-	-
Khushkhera	GU	Rajasthan	-	3.5	-	-	-
Sriganganagar	GU	Rajasthan	-	3.6	-	-	-
panipat	GU	Haryana	-	1.5	-	-	-
Roorkee	GU	Uttaranchal	-	1.8	-	-	-
Bulandshahr	GU	UP	-	2.0	-	-	-
North			15.4	26.3			
Aurangabad	GU	Bihar	-	5.6	-	-	-
Raipur	IU	Chattisgarh	5.2	3.0	19.0	30.0	-
Cuttak*	GU	Odisha	-	3.0	-	-	-
Saraikela*	GU	Jharkhand	-	2.5	-	-	-
East			5.2	14.1			
Pune**	GU	Maharashtra	-	2.0	-	-	-
West			-	2.0			
Kedla	IU	Karnataka	2.8	3.0	21.0	-	21.0
South			2.8	3.0	520.0	126.0	21.0

*expected to get commission by Dec'19

** Date not announced

Shree Cement Ltd : Financial Snapshot (Standalone)

Particulars	FY14	FY15	FY16*	FY17	FY18	FY19E	FY20E	FY21E
Volume Sales (lac tons)	142.5	161.6	142.4	205.9	225.3	252.5	313.8	345.2
Power Sales (lac Kwh)	18597	18851	17390	16583	11965	16512	16848	17016
Net reveue (INR Cr)	5887	6454	5514	8594	9833	12699	14722	16388
Growth (%)	6%	10%	-15%	56%	14%	29%	16%	11%
EBITDA (INR Cr)	1390	1344	1407	2513	2473	2806	3386	3917
EBITDA margin (%)	23.61%	20.82%	25.52%	29.24%	25.15%	22.10%	23%	24%
Net Profit (INR Cr)	787	426	1143	1339	1384	1079	1502	1791
Net Profit margin (%)	13%	7%	21%	16%	14%	9%	10%	11%
EPS	225.98	122.38	328.13	384.39	397.33	309.84	431.05	513.97
BVPS	1352.26	1514.59	1965.01	2209.76	2553.84	2841.00	3268.96	3816.89
P/E	77.5	143.2	53.4	45.6	44.1	56.5	40.6	34.1
P/BV	13.0	11.6	8.9	7.9	6.9	6.2	5.4	4.6
ROE(%)	16%	7%	17%	17%	16%	11%	13%	13%
ROCE(%)	16%	8%	13%	17%	10%	13%	18%	17%
EV/ton (\$)	505	373	345	301	262	234	204	193
EV/EBITDA (x)	45.1	46.5	44.6	24.9	26.2	23.1	19.0	16.3

Source: Company Data, SMIFS Research

Valuation

- Higher capacity utilisation and limited cement capacity addition (bound by limited clinker capacity addition) would keep the demand supply gap narrow in the Northern region. Infrastructure and affordable housing will continue to drive demand. Also, a strong demand can be expected from rural housing segment.
- Company's focus to improve realisation from increasing trade proportion in sales mix and slight reduction in pet coke and diesel prices should improve the margin further in Q4FY19. Moreover, Capacity expansion near the Eastern markets will also reduce the logistics cost to some extent.

Peer Comparison

Company	CMP	Mcap (INR Cr)	EPS			EV/EBITDA(x)			EV/ton(\$)			ROCE(%)			ROE(%)		
			FY18	FY19E	FY20E	FY18	FY19E	FY20E	FY18	FY19E	FY20E	FY18	FY19E	FY20E	FY18	FY19E	FY20E
Shree Cement	17527	61061	397.3	349.9	456.4	26.2	23.1	19.0	261	234	204	10%	13%	18%	16%	12%	14%
ACC*	1554	29144	80.2	65.9	76.2	12.8	11.5	10.3	117	108	106	14.0	16.4	18.0	9.9	11.4	12.6
Ambuja*	221	43912	11.7	9.7	11.1	10.7	9.4	8.3	133	134	135	11.3	12.8	16.4	8.6	8.9	10.9
Ultratech	3968	107495	87.3	115.1	150.6	20.3	19.2	14.7	221	201	187	10	9.7	12.5	9.5	8.2	10.4
Heidelberg	170	3981	5.9	10.1	12.1	9.8	8.9	8.2	119	116	108	14.8	21.6	24.8	12.9	18.1	18.4
India Cement	97	2993	3.5	1.8	5.4	9.2	9.4	7.3	64	63	62	5.1	4.7	5	1.9	0.9	2.0
JK Cement	802	6273	30.1	39.3	48.5	11.5	10.5	8.9	80	81	83	14.6	11.4	12.9	16.7	12.6	14.9
JK Lakshmi	343	4024	7.1	6.6	17.4	14.3	13.1	10.4	66	64	62	8.8	9.2	12.8	5.8	5.9	10.6
Star Cement	99	4203	7.9	4.2	6.6	8.6	13.2	8.5	188	178	171	21.6	17.8	20.8	22.6	16.1	16.1
Ramco Cement**	722	17015	23.61	20.7	29.5	15.8	17.6	13.3	146.3	147.1	130.7	14.0	11.0	14.0	13.7	10.8	13.8

* CY ending

** SMIFS Coverage

Source: Bloomberg, SMIFS Research

Cement sector outlook

The recent price hike in cement prices would definitely improve the profitability margins in Q4FY19. Moreover, Petcoke, a major key input, whose price has come down from peak levels of USD120-130 per ton to now USD95 per ton. According to S&P Global Platts, petcoke prices in India is expected to further come down to USD90-92 per ton levels. We estimate that this price hike if to sustain could improve realization by 5-7% and such benefit to accrue directly to bottom-line in Q4FY19. However, due to upcoming elections the cement demand could be slightly muted in Q1FY20 which could put pressure on the increased prices

To conclude, unless accompanied by adequate demand improvement from the Trade segment, such quantum of price hike may not sustain and come down slightly in short term. However, cement demand is expected to grow at 7-8% for the next 2-3 years and additional cement supply which would be limited to the clinker addition would not significantly increase the demand & supply gap. Hence, on the long term we expect the realization and return ratios to improve going forward.

We prefer ACC Ltd and Heidelberg Cement India Ltd where return ratios are high with strong financials to withstand unfavorable variables. Also, the capacity utilisation in the North is at around 85% which would benefit strategically placed players such as Shree Cements Ltd and J.K Cement from any likely price increase in the North. We also believe that if a strong Govt comes at the center, the strong pace of infrastructure spending could further strengthen and benefit some of the cheaper priced players like Ramco Cements Ltd, J.K Cement and J.K Lakshmi cement Ltd .

Appendix -1: Brand wise cement prices in the East

Month	Ultratech	Ambuja	ACC	Dalmia	Birla Corp.	Birla Gold	Average	M-oM Change
Apr-17	330	340	360	355	340	330	343	0%
May-17	335	345	360	360	345	335	347	1%
Jun-17	330	340	360	355	340	335	343	-1%
Jul-17	320	330	350	345	330	325	333	-3%
Aug-17	315	325	340	340	325	320	328	-2%
Sep-17	315	325	340	340	325	320	328	0%
Oct-17	315	325	340	340	325	320	328	0%
Nov-17	325	335	345	350	335	325	336	3%
Dec-17	325	345	345	360	345	325	341	1%
Jan-18	330	350	345	365	350	330	345	1%
Feb-18	330	350	345	365	350	330	345	0%
Mar-18	335	355	350	370	355	335	350	1%
Apr-18	335	355	350	370	355	335	350	0%
May-18	330	355	345	360	350	330	345	-1%
Jun-18	325	350	340	355	345	335	342	-1%
Jul-18	320	345	335	350	340	325	336	-2%
Aug-18	310	335	325	340	330	320	327	-3%
Sep-18	310	330	320	335	325	315	323	-1%
Oct-18	310	330	320	335	325	315	323	0%
Nov-18	310	330	320	335	325	315	323	0%
Dec-18	305	315	320	320	320	315	316	-2%
Jan-19	315	325	330	330	325	320	324	3%
Feb-19	325	335	340	335	330	330	333	3%

Source: SMIFS Research

*wholesale prices including GST

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Technical	Commodity Research	Stock Recommendation	Expected absolute returns (%) over 12 months
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		Buy	between 12% and 20%
		Accumulate	between 6% and 12%
		Hold	between 0% and 6%
		Sell	0 to <-10%
		Neutral	No Rating
		Stock Recommendation	Expected absolute returns (%) over 12 months

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