

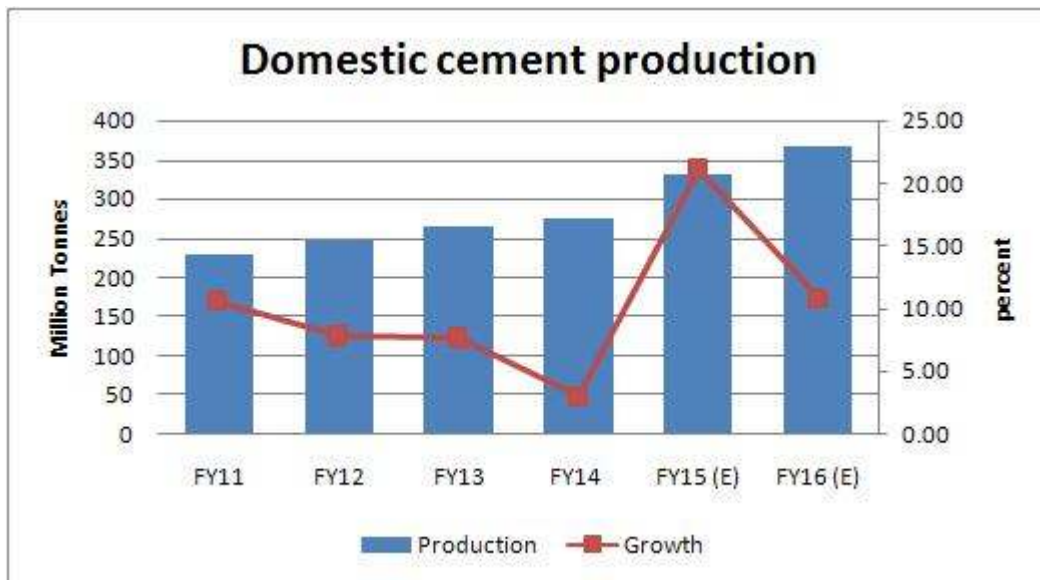
Long term funding availability for infrastructure projects to boost Cement demand

Indian cement industry plays a significant role in development of the country through the construction of infrastructure. The cement industry grew notably over the last two decades and nowadays the sector is aptly described as the next sun rise sector to Indian economy. The Indian cement Industry is very large, second only to China in terms of installed capacity at around 370 Million Tonnes (MT), and has grown at a brisk pace in recent years on back of rising infrastructure activities, increasing demand from housing sector and industries. India has huge potential in infrastructure and construction and the cement sector in India is set to receive a major boost. The Government of India is allocating funds to several infrastructure projects in the urban as well as rural areas, as per the Union Budget being announced recently in July 2014.

Also, many foreign companies are looking for investing in the Indian cement industry to cash in on the opportunities in this market. For instance, Holcim and Lafarge SA are involved in major discussions to form a potential global merger which could result in the formation of the largest cement maker in India, overtaking the current market leaders, Ultratech. In addition, there are a number of notable infrastructural projects already coming up in the country. For instance, Indian engineers are working in the Himalayas to build the world's highest railway bridge which is expected to be 35 metres taller than the Eiffel Tower when completed in 2016.

Performance of Cement Industry

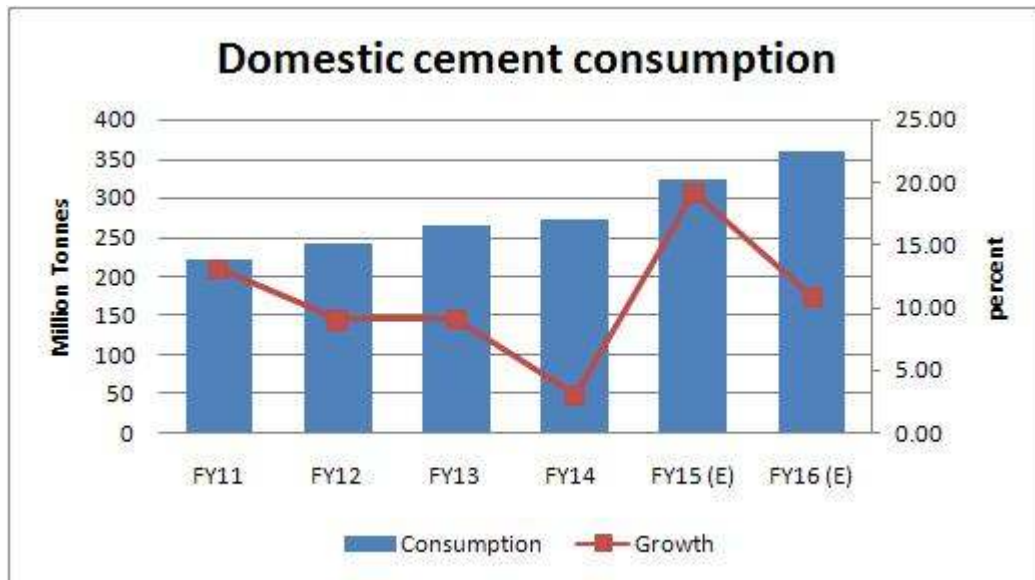
The cement production remained subdued during FY14 growing by a modest 3% during Apr-Mar 2014 as against 7.7% in the corresponding period last year. The cement demand remained weak primarily due to weak demand from end-user industries. Delays in environmental clearances for industrial and infrastructure projects and sand unavailability in some states contributed to slow growth. In fact, as against YTD (year-to-date) growth of 3%, cement production registered an even lower growth of 2% during Q3 FY14 and 1.2% in Q4 FY14 which are seasonally strong quarters for the cement industry.



However, the demand outlook for FY15 remains relatively more favourable given the new government's focus on revival of infrastructure and investment spending. The growth in FY15 will also be supported by a low base as cement production grew by merely 3% in FY14. During Apr-May 2014, cement production has grown by 7.7% Y-o-Y as against 3.9% in the corresponding period last year. Pick-up of real estate & industrial activity, infrastructure projects and overall investment cycle will remain critical for the sector over the near-term.

Cement consumption is expected to increase on higher demand

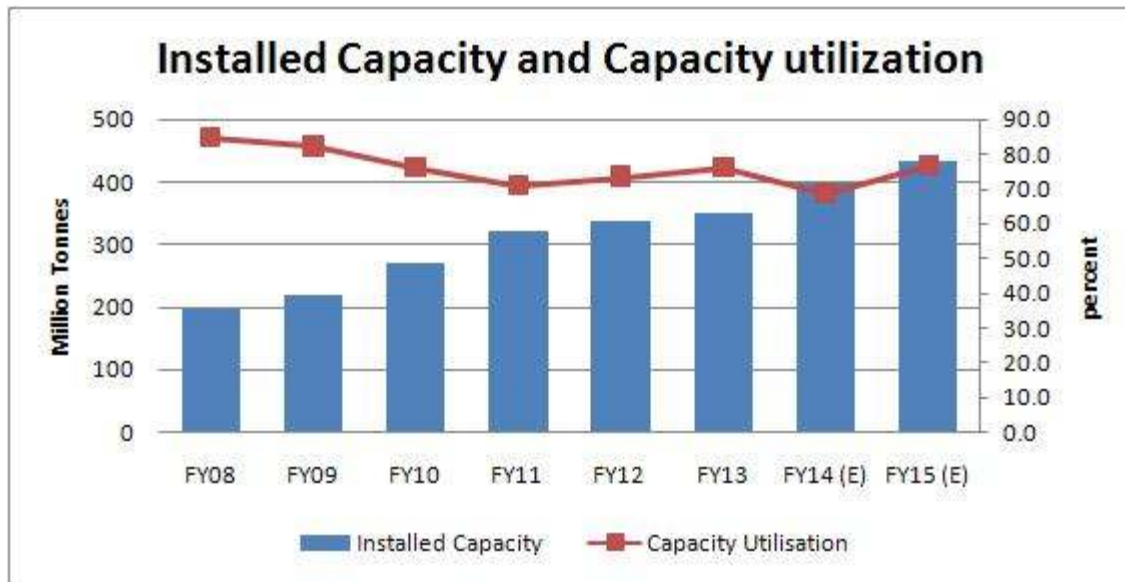
The challenging economic scenario on account of slowdown in GDP growth rate and slowdown in infrastructure activities had a cascading effect on the cement industry in the last 1-2 years. Traditionally, cement demand and GDP growth rates have had a positive correlation with cement demand to GDP growth ratio of about 1.2x; however the same has steadily declined to a low of 0.7x in FY14. Formation of stable government, budget proposals and government policy with a strong focus towards infrastructure growth and expected macro recovery is likely to augur well for housing, industrial and infrastructure sectors and in turn for the cement sector. Apart from the improved demand from future infrastructure development, pent-up demand is likely to propel the cement consumption going ahead.



Capacity addition to be moderate

Overall capacity addition to be moderate as incremental demand will be lower than incremental supply. Capacity additions will grow at a Compounded Annual growth rate (CAGR) of 6% from FY13 to FY16, more than a 4% CAGR increase in demand in the same period. Meanwhile, capacity utilization increased to 75.4% in FY13 from 73.5% in FY12. The capacity utilization for FY14 is expected to decline to 68.2%, and will increase in FY15 to around 75%.

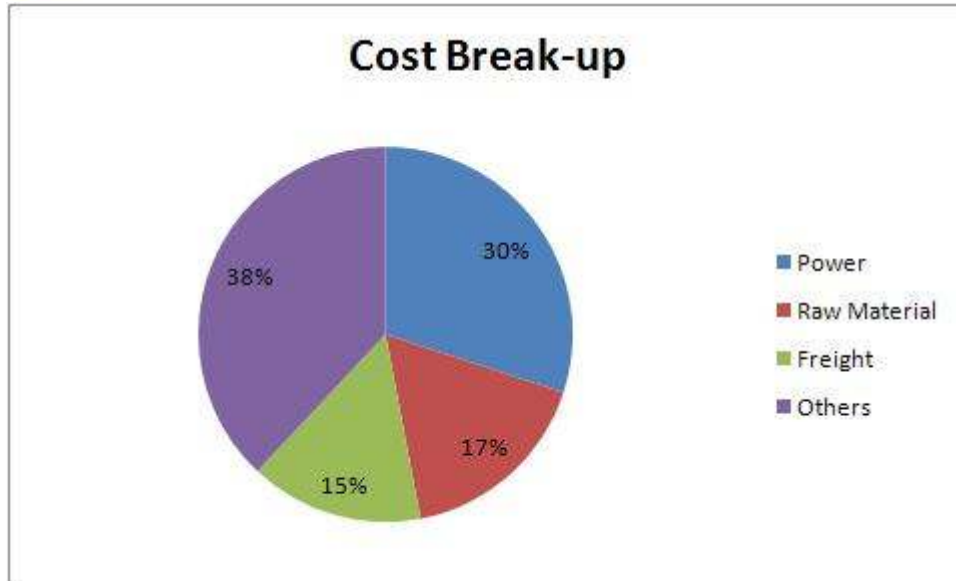
The regional imbalance is likely to continue in the near term, with southern India showing the largest demand-supply gap due to large capacity additions in the last four years. Capacity utilization for the southern region was around 62% in FY14 (FY13: 60%, FY12: 61%). The capacity utilization will be under pressure for the southern region despite moderate capacity expansion. Demand from this region was impacted during FY14 due to scanty rains and a slowdown in construction activities. Eastern India will have maximum capacity additions with nearly 15 million metric tonne to be added in the next three years.



Rising input costs impacting cement manufacturers

Increasing input costs continue to impact cement companies inversely. Over the past two years, Cement manufacturers have witnessed significant increase in freight costs on account of hike in freight rates by railways, consistent increase in diesel prices and increased dependence on costlier road transport due to shortage of railway wagons. Besides, the prices of key raw materials like, limestone and gypsum have also increased. Further, increase in domestic coal prices by CIL in May 2013, declining availability of low cost linkage coal have increased power & fuel costs.

On the flip side, declining international coal and pet coke price have provided some benefits to Indian cement companies; but the extent of this benefit has partly been offset by rupee depreciation. Given that cement prices are largely out of their control, the cement companies are now increasingly focusing on reducing their costs. Companies are taking steps to optimize their overhead costs, improve efficiency and lower consumption norms.



Companies have increasingly started using pet coke and lignite instead of expensive coal as a source of fuel and utilising waste heat gases to produce power. Steps are also being taken to optimize power consumption norms and reduce the power consumed per tonne of cement. Further, companies are focusing on using higher proportion of additives such as fly-ash and cement to bring down their cost of production. As a result, the power and fuel cost as well as raw material cost has seen some easing. However, freight costs have increased significantly in the last two years.

Cement prices in India

Cement being an essential raw material for all construction activity, an increase of around Rs 100 per bag of cement in Southern India results in the cost of construction going up by Rs 45 per sq ft of built-up area. It's a huge dampener for the construction industry as the real estate markets still remain sluggish. Hence, the real estate companies and builders association has protested against such a steep price hike.

During Apr-June 2014, the average cement price is higher by 10% in Delhi, 22% in Ahmedabad, 7% in Chandigarh as compared to average prices in the corresponding period last year. Prices in Mumbai are flat while those in South and certain parts of East India are lower on YoY basis.

North India

Cement prices in North India had seen a significant hike of Rs 50 per bag during Q4 FY14 driven by temporary supply side disruptions following closure two cement plants of Binani Cement with a total capacity of 6 MTPA in Rajasthan. The average wholesale cement price in Delhi increased from Rs 275 per bag (50 kg) in January 2014 to Rs 323 per bag in March 2014. Similarly, the average wholesale cement price in Chandigarh increased by Rs 58 per bag between Jan-Mar 2014 to Rs 334/bag. Meanwhile, the wholesale prices declined by Rs 15-30 per bag in Delhi and Chandigarh between Apr-Jun 2014.

South India

Cement manufacturers had raised prices of cement by Rs 60-100 per bag (50 kg) in the four southern states in June. Despite being the single largest producer of cement in the country, consumers of Andhra Pradesh are the worst affected with a hike of Rs 100 per bag (50 kg). The increase in Tamil Nadu and Karnataka is Rs 70 per bag and in Kerala it is Rs 60 per bag.

West India

The prices in certain parts of West India, particularly Gujarat were also impacted by the shutdown of two cement plants of Binani Cement. Wholesale prices in Ahmedabad market increased by Rs 47 per bag to Rs 300 per bag between January-March 2014. However, cement prices in these regions came under pressure in April-May 2014 following resumption of cement supply from Binani. Prices in Mumbai market continued to remain under pressure and declined by Rs 20 per bag during Jan-May 2014 due to transfer of cement from Southern markets. However, with rise in prices in South in June 2014, wholesale prices in Mumbai also increased by Rs 5-10 per bag in Jun 2014.

East India

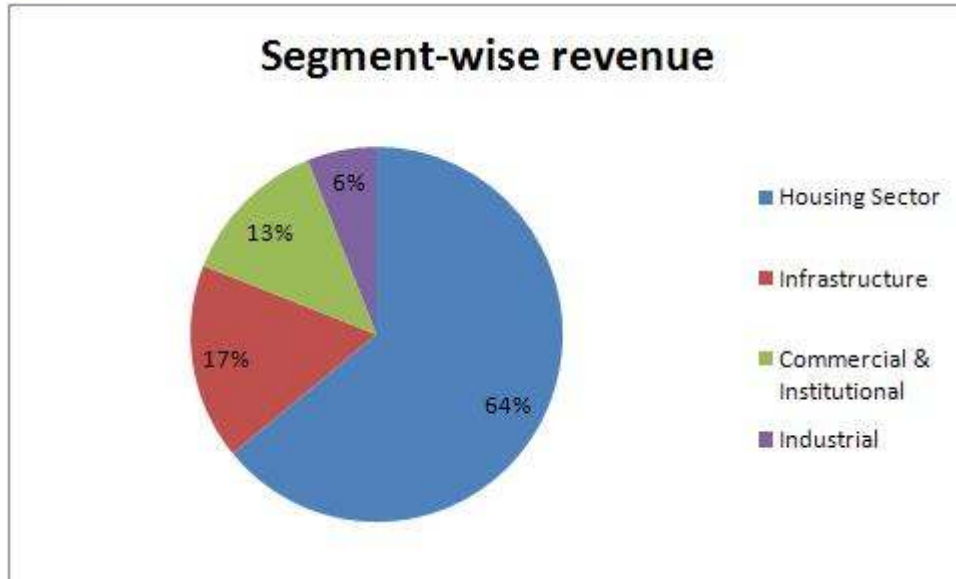
Cement prices in Eastern markets increased by Rs 20-25 per bag during Jan-June 2014 as cement companies raised prices in the busy season to recover the rising costs.

Hopes pinned on infra and housing revival

Indian cement industry can be divided into four major segments viz; housing segment, infrastructure segment, commercial & institutional segment and industrial segment. Among these segment, housing is the largest segment of the industry accounting for around 64% of the total cement demand. Infrastructure represent around 17% share in the domestic cement consumption, while commercial & institutional and industrial segment accounts 13% and 6% share in cement consumption.

Weakness in housing demand, cash flow crunch and bottlenecks in the infrastructure sector slowed construction activity, hurting cement sales in the past few years. Higher tax has resulted in one of the lowest per capita consumption of cement.

Infrastructure and commercial segments account for around 30% of cement demand and a recovery in these sectors are likely to contribute 10 percentage points to cement growth over 2014 to 2017. The new government's manifesto made a lot of promises, such as creation of industrial corridors and highways connecting satellite towns to twin cities. Any announcement on the much talked about Diamond Quadrilateral project to create a high-speed train network, building and modernizing airports, and inter-linking rivers will help cement demand.



The government may also give some impetus for implementing the eastern and western dedicated freight corridor. Moreover, it is expected that the dedicated freight corridor will increase annual cement demand by 1.5% over the next 5-6 years on the back of 21 million tonnes (mt) of consumption. Announcements to promote low-cost housing, credit, subsidy schemes on bank interest rates and easing the land acquisition norms will also be positive for the sector. Many projects are stalled because of land acquisition delays and other regulatory hurdles. Unless the government simplifies the clearance process and provides incentives for infrastructure funding, it will be negative for the sector.

Outlook

FY14 was a challenging year for the cement industry, with cement consumption increasing by about 3.5% as compared with 5.3% in FY13 and 6.7% in FY12 on account of slowdown in infrastructure, industrial and real estate projects. Consequently, cement prices also remained under pressure for major part of the year. Lower realization, higher input costs and freight expenses impacted the operating margins of majority of the players significantly. Despite challenging industry scenario in FY14, most of the cement players were able to maintain healthy liquidity in terms of cash and cash equivalents and unutilised working capital limits (especially pan India, northern and eastern players) and moderate capital structure.

While the cement industry would continue to witness cyclical trends due to the inherent nature of the industry, the long-term outlook for the cement sector is expected to be stable as several initiatives announced to promote infrastructure and housing investment in Union Budget are likely to have a positive impact on cement demand. Increased provision under Rural Housing Fund and interest deduction on housing loans will boost urban and rural housing demand and in turn demand for cement. Further, government measures to promote investment in ports, roads, airports and other infrastructure projects are also likely to support cement demand. Cement companies are also likely to benefit from the increase in long term funding availability for infrastructure projects which is likely to facilitate more investment in these sectors.

Companies Financial Data In Industry

COMPANY NAME	CMP	MCAP	BOOK VALUE	DIV. YEILD %	TTM EPS	TTM PE
Shree Cement Ltd.	8303.75	28927.96	1352.25	0.26	225.98	36.75
Ultratech Cement Ltd.	2646.05	72604.81	645.76	0.34	76.44	34.62
ACC Ltd.	1429.15	26831.63	433.29	2.10	55.33	25.83
HIL Ltd.	653.40	487.60	556.42	0.77	36.23	18.03
Birla Corporation Ltd.	475.80	3663.91	340.01	1.26	23.80	19.99
OCL India Ltd.	309.65	1761.92	201.42	1.29	16.10	19.23
JK Cement Ltd.	510.65	3570.84	226.15	0.59	14.90	34.28
Kakatiya Cement Sugar & Industries Ltd.	107.90	83.88	225.49	2.50	10.88	9.92
Indian Hume Pipe Company Ltd.	298.90	724.04	107.31	0.80	10.53	28.38
JK Lakshmi Cement Ltd.	332.25	3909.59	112.99	0.60	10.01	33.20
Everest Industries Ltd.	254.20	387.04	206.35	0.98	9.89	25.70
Ambuja Cements Ltd.	211.85	32805.59	65.24	1.70	9.11	23.25
Mangalam Cement Ltd.	238.85	637.58	192.99	1.26	8.92	26.77
Saurashtra Cement Ltd.	50.50	258.51	34.54	0.00	6.57	7.69
Visaka Industries Ltd.	117.80	187.08	216.95	2.12	5.95	19.79
Keshav Cements Ltd.	16.90	8.66	29.37	0.00	5.66	2.98
Deccan Cements Ltd.	381.30	267.05	321.11	0.31	4.87	78.29
Orient Cement Ltd.	122.35	2506.57	42.16	1.23	4.81	25.43
The Ramco Cements Ltd.	318.75	7585.27	105.83	0.31	4.42	72.17
Century Textiles & Industries Ltd.	547.30	5092.39	194.95	1.00	3.39	161.36
Bansal Roofing Products Ltd.	33.50	7.36	12.78	0.00	2.92	11.48
Sanghi Industries Ltd.	52.55	1155.99	40.44	0.00	2.25	23.32
Heidelberg Cement India Ltd.	81.15	1838.97	38.33	0.00	1.09	74.39
Star Ferro and Cement Ltd.	60.00	1333.04	5.24	0.55	0.92	65.03
Gujarat Sidhee Cement Ltd.	34.10	144.43	36.25	0.00	0.78	43.54
Barak Cement Ltd.	13.60	30.14	37.94	0.00	0.41	33.52
Burnpur Cement Ltd.	12.93	97.69	13.08	0.00	0.32	40.74
Udaipur Cement Works Ltd.	16.00	472.33	0.67	0.00	0.16	101.16
Shiva Cement Ltd.	4.36	81.53	5.13	0.00	0.13	33.76
KCP Ltd.	48.60	626.56	26.98	0.21	0.06	835.41
Jaiprakash Associates Ltd.	27.15	6604.12	61.33	0.00	-0.01	0.00
Prism Cement Ltd.	69.90	3518.46	20.29	0.00	-0.41	0.00
Dalmia Bharat Sugar & Industries Ltd.	20.60	166.73	57.08	0.00	-0.53	0.00
Orient Paper & Industries Ltd.	29.15	597.19	19.75	0.34	-0.89	0.00
Ramco Industries Ltd.	70.80	613.57	53.98	0.35	-1.04	0.00
Shree Digvijay Cement Company Ltd.	21.85	308.90	14.93	0.00	-1.13	0.00
The India Cements Ltd.	113.45	3484.94	113.63	1.76	-1.81	0.00
Andhra Cements Ltd.	9.85	289.12	6.97	0.00	-2.65	0.00



Sector Cement Industry

Sahyadri Industries Ltd.	67.25	64.30	124.84	0.74	-2.89	0.00
Panyam Cements & Mineral Industries Ltd.	34.00	54.46	13.79	0.00	-3.03	0.00
Bheema Cements Ltd.	12.20	34.54	33.85	0.00	-4.76	0.00
NCL Industries Ltd.	34.60	127.10	33.70	2.89	-13.00	0.00
Anjani Portland Cement Ltd.	71.95	132.31	28.03	0.00	-14.48	0.00
Sagar Cements Ltd.	325.00	565.11	133.58	0.00	-16.96	0.00

Source – Ace Equity

Disclaimer

This report is for private circulation within the Indira Group. This report is strictly confidential and for information of the selected recipient only and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form. This report should not be construed as an offer or solicitation to buy or sell any securities or any interest in securities. It does not constitute a personal recommendation or take into account the particular investment objectives, financial situations, or any such factor. The information, opinions estimates and forecasts contained here have been obtained from, or are based upon, sources we believe to be reliable, but no representation of warranty, express or implied, is made by us to their accuracy or completeness. Opinions expressed are our current opinions as of the date appearing on this material only and are subject to change without notice.