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Cement industry margins set to contract in FY23; price hikes imminent

NEW DELHI: Cement companies are expected to register a 8-9% rise in their volumes in FY23 on strong demand, but operating profit margin may decline due to high input costs, CareEdge Ratings said on Monday.
“Driven by the housing and infrastructure sectors, the cement industry has witnessed a V-shaped recovery and healthy growth in FY22. At 350 million tonnes, the demand surpassed pre-Covid levels of 331 MT in FY19 and is expected to grow by 8-9% y-o-y in FY23," the report said.

“Increased government spending on infrastructure and a pickup in real estate is likely to support demand further," it said.

According to the rating agency, the combined impact of all input costs, primarily that of fuel, is expected to push up the cost for cement players by ₹350 to ₹400 per tonne year-on-year. While there is heightened focus on efficiency measures, CareEdge Ratings said, it believes it will still be difficult to fully offset higher energy costs.

CareEdge expects cement prices at pan-India level to rise an average 3.5-4% on the high base of FY22. Though this is not enough to completely offset the cost pressures but these partial hikes in realisations will limit the contraction in operating margin to a certain extent.

While players have announced price hikes across regions in November in the range of ₹15-20 per bag, the absorption and sustainability of these hikes are key monitorables.
"In the present circumstances where the sector is grappling with the higher fuel cost, a sustained increase in prices without impacting the demand momentum stands critical for the operational performance of the players in the near term. An increase of approximately ₹25-30 per bag would be required to offset the cost inflation on a year-to-year basis and a hike of ₹45-50 per bag is required to restore the profitability back to FY21 levels," CareEdge Ratings said.

"The moderation in the EBITDA margins amid the cost pressures and after considering the year-on-year price hikes to the tune of 3.5-4% will be in the range of 320-380 bps y-o-y in FY23 or an EBITDA per tonne impact of ₹180-200," it added.

"The macros of the cement industry remain stable in the long term, driven by demand from the urban housing sectors, upcoming infrastructure projects as well as generous rural demand, though presently the sector is riddled with the cost-side issues. In the present circumstances where the sector is grappling with the higher fuel cost, a sustained increase in prices without impacting the demand momentum stands critical for the operational performance of the players in the near term," said Ravleen Sethi, associate director, CareEdge.

"While the credit metrics of the industry largely remain stable due to the net cash positive position of the large players, medium-sized players are likely to witness more moderation in the credit metrics due to subdued profitability and capex-related debt, which is expected to come on their balance sheets. The players need to take price hikes in a gradual manner such that it should not weigh down on demand revival."

"An increase of approximately ₹25-30 per bag would be required to offset the cost inflation on a year-to-year basis and a hike of ₹45-50 per bag is required to restore the profitability back to FY21 levels," she added.