The Indian Cement Industry – "Cement demand to grow at a CAGR of 7.9 per cent in the period FY13-16…"

The cement industry witnessed a dismal demand growth in past few years. The slowdown in the real estate sector and delay in takeoff of various infrastructural projects in the period FY11-13 took a toll on the cement demand. Spiralling cost of capital, delays in execution of both infrastructure as well as industrial projects on account of land acquisition & environmental clearance hurdles and the economic slowdown adversely affected the offtake of cement. In the period FY11-13, cement consumption grew at CAGR of mere 5.6 per cent compared to CAGR of 9.9 per cent in the period FY 07-10. The multiplier of cement demand growth to the GDP growth declined below one in FY 11 & FY 12.

CARE Research expects the cement demand to recover gradually. The increasing focus of the Government of India (GoI) on strengthening infrastructure, promotion of low-cost affordable housing, lowering trend of interest rates and expected revival in the overall economic growth will provide some respite to the cement demand. Also, the pre-election spending, increase in ECB limits for low cost housing sector, ongoing consideration to provide infrastructure status to the affordable housing segment will drive the growth of cement demand. The economic growth is expected to revive from 5 per cent in FY 13 to about 7.8 per cent in FY 16. Accordingly, CARE Research estimates the cement demand to grow at a CAGR of about 7.9 per cent in the period FY13-16.

Housing demand to drive the cement consumption…

The real estate sector continues to dominate as the largest cement consuming sector in the country. Almost 55-60 per cent of the total cement demand is derived from the real estate sector. Over last couple of years, the real estate market was confronted with slowdown. Elevated real estate prices led by the rise in construction cost and rising trend of interest rates had dampened the real estate demand across the country. The deployment of funds by banks to the real estate also showed a drop.

Going ahead, various measures taken by the government to promote affordable housing and falling trend of interest rates are expected to drive growth of housing demand. As per the report of the technical committee constituted by Ministry of Housing and Poverty Alleviation, urban areas in the country have a shortage of about 19 million houses. CARE Research estimates that new dwellings in the urban region would translate into cement demand of about 120 mn tonnes in the next three to four years. Apart from this, GoI has estimated that the rural housing demand is likely to cross a number of 40 million by the end of FY17. Accordingly, the rural housing segment is expected to consume about 150-170 mn tonnes of cement in next three to four years.

Cement demand from infrastructure space to catch pace…

Over the period of past two Five Year Plans, the investment in infrastructure as a percentage of GDP has been on rise. It has increased from a level of 5 per cent of GDP in the 10th Five Year Plan to about 7.2 per cent in the 11th Plan. In the 12th Five Year Plan, GoI has set an ambitious target of increasing the proportion of infrastructure investment to about 9.1 per cent of the GDP. This translates into a massive investment to the tune of about Rs. 51,464 bn during the 12th Five Year Plan (FY 13-17). The huge investment planned in the 12th Five Year Plan augurs well for the cement industry. Based on scheduled completion and the construction intensity of these projects, CARE Research has estimated that various sub-sectors under the infrastructure sector will derive a cement demand of about 145 mn tonnes in next three years.

The pace of capacity addition to decelerate …

Over the past few years, the cement industry has witnessed huge capacity addition. The capacity has increased from 219 mn tonnes in FY09 to 325 mn tonnes in FY13, registering a CAGR of 10.4 per cent. Consequently, the gap between the demand and supply has increased substantially. CARE Research believes that given the huge surplus situation prevailing in the industry, the pace of capacity addition will decelerate going ahead. CARE Research has estimated that the industry will add capacity of about 66 mn tonnes during the period of FY14-16. On account of huge capacity addition, the utilisation rate of the industry dropped from the peak of 93 per cent in FY07 to 73 per cent in FY13. CARE Research believes that going forward, the capacity utilisation rate of the industry will improve gradually given the slowdown in pace of capacity addition and gradual recovery in cement demand. CARE Research expects the overall operating rate of the industry to increase to 76 per cent in FY16.

Cement prices to remain elevated, but escalation in cost will exert pressure on margins in FY14…

The power & fuel cost and freight cost are the major cost components of the cement industry. In FY13, the power & fuel cost and freight cost together accounted for about 55 per cent of the total cost.

No respite from rise in Power and Fuel cost…

In FY13, the international coal prices declined by about 22 per cent on a YoY basis. However, on account of rupee depreciation, the average cost of the imported coal remained flat on a YoY basis in FY13. The per tonne power and fuel cost of the industry increased by about 5 per cent on a YoY basis in FY13.

CARE Research has estimated that the per tonne power and fuel cost of the industry will increase by about 10 per cent on a YoY basis in FY14. The international coal prices are expected remain stable and not soften further in FY14. The coal shortage in the country and limited availability of coal through linkage will make it inevitable for the cement industry to procure coal through imports and open market purchases at higher rates in this fiscal.

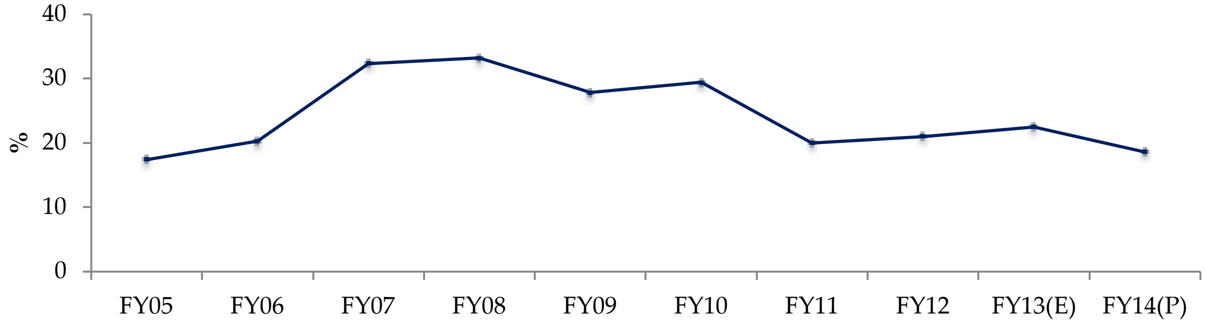
Hike in rail freight & partial decontrol of diesel prices to push freight cost upwards…

The cement industry, on an average, dispatches more than 60 per cent of cement by road followed by the rail at 35 per cent and rest by sea. In FY13, the average diesel price increased from Rs.43.5 per litre in April 2012 to Rs. 52 per litre in March 2013. Consequently, the per tonne freight cost of the industry increased by about 15 per cent on a YoY basis in FY13. This was also on account of the increase in railway freight charges, hike in busy season charge and development surcharge.

Firm crude oil prices in the international market and deregulation of diesel prices are expected to keep price of diesel elevated in FY14. In the recent budget, Railway hiked the freight rate (for distance 800-850 km - it increased from Rs. 1,038 per tonne to Rs. 1,096 per tonne). This will push the freight cost of the industry upwards in FY14. CARE Research has estimated that the per tonne freight cost of the industry will increase by about 15 per cent on a YoY basis in FY14.

In FY13, the cement industry witnessed a marginal improvement in the PBDIT margin despite the rise in the cost. The industry was able to pass on the increased cost burden to the consumers on the back of the supply discipline followed by the cement players in this fiscal. In FY13, the per tonne total expenditure of the industry increased by 13 per cent on a YoY basis while the per tonne realization increased by about 15 per cent on a YoY basis. Consequently, the PBDIT margin of the industry improved marginally by 2 per cent to reach a level of 22.5 per cent in FY 13.

Trend of PBDIT margin

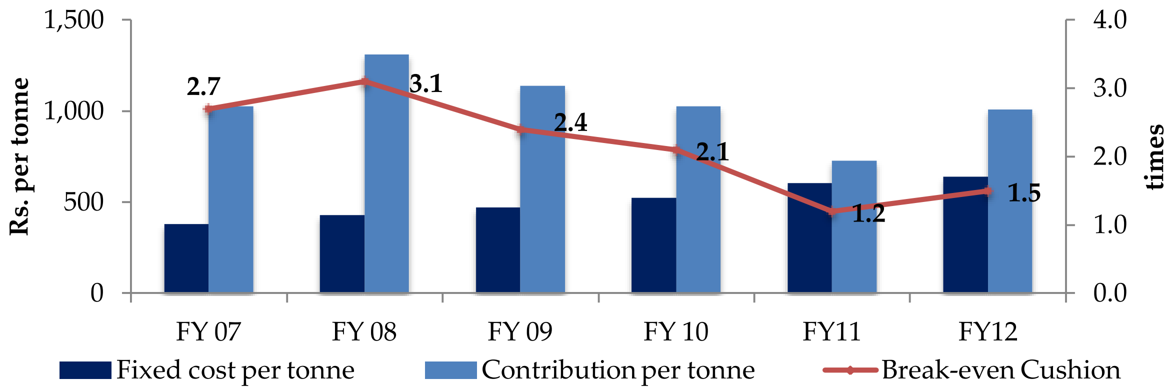


Source: CARE Research

Given the recovery expected in the demand, the cement prices are expected to remain elevated in FY14. However, the per tonne total expenditure of the industry is expected to rise by about 10 per cent on a YoY basis in FY14, mainly due to the increase in power & fuel and freight costs. This would exert pressure on the PBDIT margin in FY14. CARE Research expects the PBDIT margin of the industry to decline to 19 per cent in FY14.

Production discipline to sustain, given the comfortable break even cushion…

Break-even Cushion



Source: CARE Research
Break-even cushion is defined as the ratio of overall capacity utilisation rate of the industry to the utilisation rate at the break-even point in a particular year.

During the period FY06-08, the industry had witnessed rise in the break-even cushion value on the back of substantial rise in realisation. However, post FY08, the breakeven cushion of the industry started declining on account of slow down in the pace of growth in realization led by the surplus capacity coupled with the increase in cost. Even though, the break even cushion dropped below 2 times, it was at a comfortable level of 1.5 times in FY12. CARE Research expects the break even cushion to rise further on account of slowing capacity addition and revival in cement demand expected over next couple of years.

To subscribe to our report on '**Indian Cement Industry – 2013**', please contact careresearch@careratings.com.

Click on the icon to see the ***Table of Contents*** and ***Brochure*** of the report.

Contact:

Revati Kasture
Head - CARE Research
revati.kasture@careratings.com

Chaitanya Raut
Sr. Manager
chaitanya.raut@careratings.com

Manohar Annappanavar
Manager
manohar.annappanavar@careratings.com