CARE Ratings
Professional Risk Opinion

# Cement Industry: April-December update

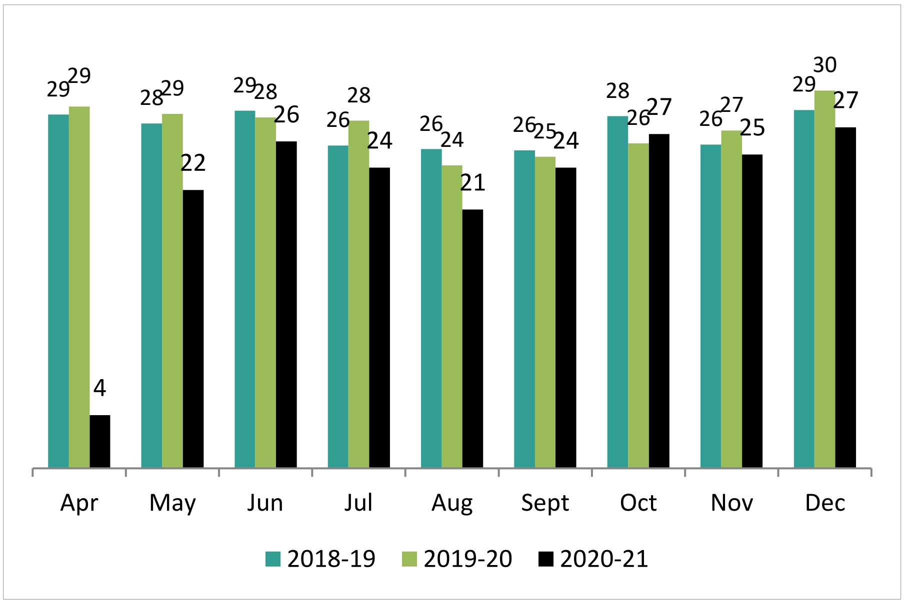
**February 8, 2021 I Industry Research**

Demand-Supply during April-December 2020 i.e. 9M-FY21

**Domestic Production and Capacity Utilisation**

**Table and Chart 1: Domestic Production of Cement (Unit: Million tonnes)**

| | Production | Change (y-o-y) |
|---|---|---|
| **2018-19** | 246 | 13.9% |
| **2019-20** | 247 | 0.7% |
| **2020-21** | 202 | -18.3% |




Source: Office of the economic advisor, CARE Ratings

Cement production fell to a 4-month low falling by 9.7% in December 2020 compared with -7.3% in November 2020 and 5.4% in December 2019. Fall in production could indicate waning pent-up demand and normalising of operations in the infrastructure space.

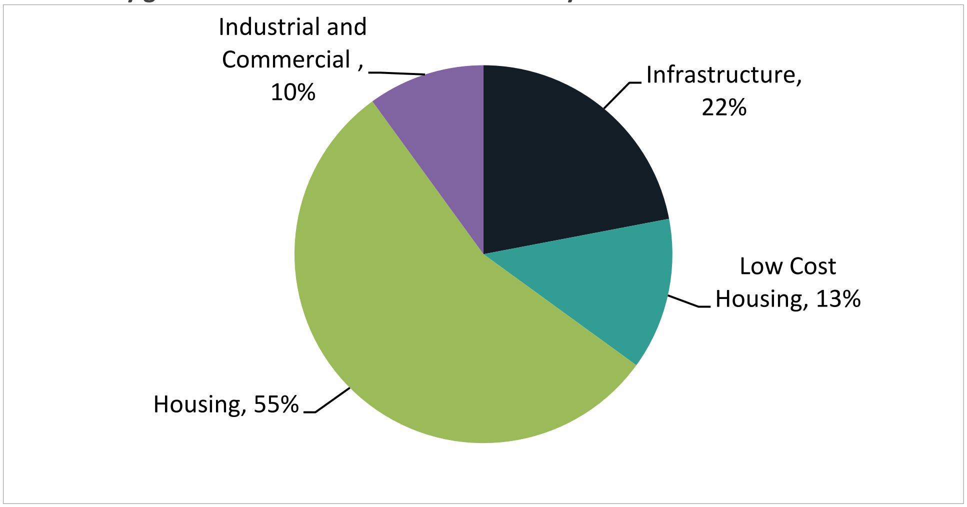
Cumulatively domestic cement production has fallen by 18.3% during 9M-FY21 compared with the 13.9% growth and 0.7% growth achieved during 9M-FY19 and 9M-FY20. Outbreak of the COVID-19 pandemic in the Indian sub-continent which forced the government to announce a nation-wide lockdown, 25th March 2020 onwards has majorly affected the cumulative domestic cement production. The nationwide lockdown had come at the time when construction activities are at its peak.

Capacity utilisation of domestic manufacturers has been around 49.5% during 9M-FY21 as units have been operating at sub-par capacities along with staggered shifts but has increased from it being 45% during H1-FY21 47% during 7M-FY21 and 48.5% during 8M-FY21. Cement manufacturers had cut down or deferred CAPEX expenditure given the fall in demand and also as companies looked to conserve their capital/cash flows but lately many of the players have been announcing CAPEX expansion of CAPEX guidance plans.

**Trend in Demand Drivers for the Cement Industry**

Cement demand is closely linked to the overall economic growth, particularly of the housing and infrastructure sector. Increasing demand from affordable housing and construction work for other government infrastructure projects like roads, metros, airports, irrigation etc. are demand drivers which support cement demand.

**Chart 2: Key growth drivers for the Cement Industry**




Source: CARE Ratings, Company Filings

Amidst the pandemic cement consumption is growing strong in the rural, semi-urban and retail markets. Over the months, cement demand is being driven by rural India due to better labour availability; there has been an increase in construction of rural infrastructure and low cost housing. Rural demand is usually w.r.t. retail market largely which is the housing and repair and modification market. Now as the economy has unlocked, there has been a steady pick up in housing and government infrastructure projects which has resulted in reviving demand across our markets even in urban India. Project execution too has picked up pace once again following the receding of the monsoon season.

- Real Estate markets in Tier-1 cities has been opening up though it has been very slow but is garnering good traction as with the advent of "work from home", consumers want to buy their own or a larger space.
  - Realtors are also focusing on completing existing or stalled projects.
- Cement demand in terms of low cost housing is showing green shoots. Cheap housing loans, extension of the CLSS and the need for space is also spurring some demand.
  - As part of the Atmanirbhar Bharat package, the government has also made a provision for an additional outlay of Rs 18,000 crore for the urban housing scheme (PMAY-U). The allocated amount is over and above the Budget Estimates for 2020-21 (Rs 8,000 crore) and will be through additional allocation and extra-budgetary resources.
  - The following announcement is to help complete real estate projects in the affordable housing segment. It is to help start work on 12 lakh houses as well as complete 18 lakh houses, create 78 lakh new jobs and augment the demand for steel and cement.
- Demand is also getting influenced by the non-trade segment gaining momentum with the resumption of construction work of institutional infrastructure projects such as roadways and metros.
  - MORTH has constructed 7,767 km of National Highways upto December 2020 compared with 6,940 km constructed upto December , 2019.

**Financials**

The financials of 22 cement manufactures have been analysed here. The cement industry is dependent on natural resources and is highly energy intensive. Natural resources like limestone, coal and minerals are essential to produce cement. The industry needs to ensure the continuous supply of these materials at an optimum cost and quality. A significant factor which aids the growth of this sector is the ready availability of limestone and coal.

**Table 2: Financials of 22 Cement companies (Unit: % change)**

| | y-o-y | Q3-FY21 | | y-o-y | |
|---|---|---|---|---|---|
| | Q3-FY20 | y-o-y | q-o-q | 9M-FY20 | 9M-FY21 |
| Net Sales | -1.7% | 14.0% | 16.0% | 3.1% | -5.8% |
| Total Expenditure | -4.8% | 5.0% | 16.3% | -2.1% | -10.9% |
| Cost of Services & Raw Materials | -9.3% | 11.1% | 20.8% | -6.8% | -10.9% |
| Electricity Power & Fuel Cost | -19.5% | 11.0% | 25.1% | -9.5% | -17.1% |
| Selling & Distribution Expenses | -7.4% | 16.9% | 22.3% | -4.3% | -5.8% |
| Operating Profit | 14.0% | 59.5% | 16.5% | 30.9% | 16.8% |
| Profit after tax | 15.4% | 200.5% | 34.5% | 80.7% | 45.5% |

| | Q3-FY20 | Q2-FY21 | Q3-FY21 | 9M-FY20 | 9M-FY21 |
|---|---|---|---|---|---|
| OPM (%) | 18.5 | 25.8 | 25.9 | 21.2 | 26.2 |
| NPM (%) | 4.1 | 6.5 | 7.8 | 4.8 | 6.4 |
| ICR (times) | 4.3 | 9.8 | 11.4 | 6.5 | 10.1 |

Source: ACE Equity, CARE Ratings

Due to various cost rationalisation measures and overhead controls undertaken by cement manufacturers, there has been an increase in the operating profit margins (OPM), net profit margins (NPM) and interest coverage ratio during Q3-FY21 and 9M-FY21. The overall sales revenue has increased by 14% during Q3-FY21 y-o-y but has declined sharply by 5.8% during 9M-FY21 y-o-y.

- There has been an uptick in Real Estate activities in Tier II, Tier III towns which initially was downbeat, but has started showing signs of recovery, aided by the current low-interest cost regime, various benefits being given by the authorities to home buyers as well as to developers has boosted the real estate sector.
- Rural demand has sustained considering the monsoons have been favourable in most parts of the country.
- Pick up in housing and institutional infrastructure projects has resulted in an increase in demand across our markets during Q3-FY21.

Overall expenditure has increased by 5% during Q3-FY21 but due to supply chain management, contract renegotiations, third party spends and fuel efficiency overall expenditure has fallen by 10.9% during 9M-FY21. This y-o-y decline has greatly benefitted the industry largely given the sharp fall in the topline numbers during the first half of current financial year. Selling & distribution, cost of raw materials and fuel/electricity cost accounted for 65%-66% of the total expenses for cement manufacturers during the current financial year.

- Electricity and fuel cost has increased by 11% after months of subdued oil prices (9M-FY21 electricity and fuel has declined by 17.1%). During Q3-FY21 petcoke prices have increased by 12.8% due to limited availability and increase in demand from Latin America and the Mediterranean. Many cement manufacturers in fact are also switching from use of petcoke to international coal which has high calorific value and is cheaper than pet coke but coal prices too have increased by 1.6% during the quarter due to the production and logistic disruption, strong Chinese winter demand amidst ban on Australian coal as well.
- Logistics cost for cement industry has increased by 16.9% (selling and distribution) despite the railways not charging the busy season surcharge. Prices have increased due to the increase in price of diesel during Q2-FY21 but on the other hand during 9M-FY21 it fell by 5.8% on account of renegotiation of contracts, logistic efficiency as well as network optimization.
- Cost of raw materials has increased by 11.1% during Q3-FY21 even though cost of limestone has declined by 13.5% during quarter.

**Outlook for FY21**

Going forward, outlook for cement industry in FY22 seems sanguine due to the government's thrust towards infrastructure creation and development and it being the propeller of growth in the economy going forward. Budgetary allocation made towards roads development, housing and rural infrastructure is slated to lead to an increase in demand for the months to come but at the moment the industry is riddled with the COVID-19 pandemic and issues associated with it.

Cement production is however to fall sharply by 12%-14% during FY21 and capacity utilization is to be around 50-55%.This will be the steepest ever fall in production (and capacity utilisation) that the industry has ever witnessed. Production of cement has grown by 13.3% during FY19 and fallen by 0.8% during FY20. Cement production is usually closely in-line with demand which is also poised to fall during FY21 even though the operations are still picking up. The industry could benefit with the pent up demand phenomena as the economy has been on an unlock mode.

**Supply side issues**

- Cement manufacturers have resumed work but is still plagued with limited manpower and many plants are still operating on staggered shifts.
- Cement manufactures are not expected to make any additions to the existing CAPEX and given the limited

demand present there have also been CAPEX deferral announcements as well.

- Production is trying to gain momentum as the reverse migration of workers had led to a standstill in operations, disrupting the entire supply chain operations. Certain groups of labourers have been returning but a major part of the labour workforce will only come back after all the agri-work is over.

**Demand side issues**

Going forward the cement industry demand is slowly improving from the disruption created from COVID-19 due pick-up in government spends on infrastructure and affordable housing along with rising rural consumption. We believe rural demand will be the major driver for cement considering the monsoons have been favourable in most part of the country. This could translate in an inflow of cash in the rural economy which could commensurate in infrastructure creation thus augmenting cement demand.

- Given how fiscally strained the government finances are at the moment, not all infrastructure projects have resumed construction which thus affecting the demand for cement.
- Growth in the housing segment which forms about 68% of cement demand (including low cost housing) is likely to be impacted as commercial & new residential launches will not be able to fully recover during FY21 as realtors are not undertaking new projects as they are only focusing on completing existing projects and clearing existing inventory in the current financial year.

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