

Cement Sector

25 March 2019

Price Momentum Fails To Keep Pace As Demand Falters

All-India retail cement prices fell marginally by 1% MoM, although they rose 6% YoY, to Rs322/bag in March 2019 (from Rs326/bag in February 2019 and Rs305/bag in March 2018). Prices rose YoY in all regions except eastern region, but the pace was higher in southern region. However, on MoM basis, the prices showed a mixed performance with a decline in southern and western regions by 1%-3% (the upward movement was sharp in February 2019), while prices in central and northern regions rose in March 2019 in the range of 1%-2%. Price weakness continued in eastern region. Our channel check indicated that the upward price movement (~2%) in central region (comprising Madhya Pradesh or MP and Uttar Pradesh or UP) was supported by healthy despatches and hence prices are unlikely to weaken in the short term. Cement demand, which was subdued in MP in the recent past because of assembly elections and formation of the new government, is gaining momentum as the new government has given fresh impetus to infrastructure projects in the state. UP continues to be the best cement market with continued healthy pricing and despatches going hand-in-hand. However, price gains in northern region (~1%) are not backed by healthy demand, but largely because of curtailed supply. Price movement lacks the necessary strength in the region and can weaken given the next few months of subdued demand because of the forthcoming general elections in India.

Our interaction with the channels indicated that strong demand in southern region lost its momentum, albeit marginally, because of a steep price hike in February 2019. Effectively, except for Bengaluru (where the prices were maintained MoM) all major centres in southern region including Hyderabad and Chennai saw prices weakening by Rs20/bag and Rs5/bag, respectively. Demand pick-up YoY, however, helped southern region-based companies to improve their capacity utilisation. Cement demand in January 2019 (latest available official data) has shown a growth of ~11.0% YoY. YTD (April-January) cement demand growth was ~13.6% also because of a weak base advantage in 1HFY19. Excluding southern region, the pricing scenario YoY was in lower single digits with a 3%-5% uptick, despite healthy pan-India demand, as supply continues to surpass demand, thereby helping incremental demand to be absorbed without any real pricing pressure. In southern region, the demand-supply imbalance was even acute (SS>DD), but restricted supply helped the prices to jump 18.5% YoY in March 2019. However, prices in southern region in FY19 declined 2% YoY. Our channel check, except for central region, indicated limited buoyancy in respect of sustainability of price hike. The hike in prices and relative tapering of costs (largely logistic costs), however, may benefit cement companies in our coverage universe in 4QFY19 as the cap on EBITDA margin is likely to go off, but it is likely to be for a limited period.

Our channel check (sample size of ~22 cement dealers) across India indicates that pan-India demand has gathered pace across regions, largely driven by government initiatives like infrastructure and low-cost housing projects. Southern states have shown strong demand revival, but could not sustain the high price hike in February 2019. Central region continued with its strong growth, contributed by the twin states of MP and UP and currently remains to be the best cement market in India. In eastern region, demand pick-up continues to be strong (barring the current festive season of Holi) in Bihar/Jharkhand, but Odisha (because of assembly elections) and West Bengal continued to remain tepid. Although the interior western region (largely rural) points towards strong demand, urban-centric regions (cities like Mumbai and Ahmedabad) continue to face weak demand because of sustained weakness in organised real estate segment and dull private as well as commercial segment demand. The only respite in this region was strong demand push from infrastructure segment (road and irrigation projects). The northern region recently witnessed demand revival, although the real pick-up is likely to be after the general elections. Our channel check indicates that the busy-quarter demand that persists in 4Q of a financial year has been repeated in FY19, but the new structural uptick in demand is expected only after the general elections and its outcome. Demand will be largely supported by projects under implementation by state and central governments. However, for any strong demand uptick political clarity will be a key trigger. Cement prices will be under pressure because of the shift in demand towards Ordinary Portland Cement (OPC) from Portland Pozzolana Cement (PPC), demand from project (non-trade) segment and intense competition because of excess supply. Further, consolidation in cement industry with market leader UltraTech Cement (UTCEM) continuing to acquire/bid for assets is likely to keep cement prices non-remunerative. This is also likely to impact the operations of relatively weak players in the region where UTCEM is aggressively pushing despatches. We continue to prefer southern region-based cement companies including The Ramco Cements (TRCL) and JK Cement among mid-size companies and HeidelbergCement in the small size group.

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Prices a mixed bag in March 2019

Region (Rs/bag)	Mar-19	Feb-19	Mar-18	3MMA YoY Change (%)	3MMA QoQ Change (%)
Eastern	311	315	318	(1.4)	0.8
Western	305	309	298	4.4	(0.0)
Northern	303	298	293	0.7	(1.9)
Central	320	318	306	0.5	(2.3)
Southern	365	379	308	(0.1)	4.4
All India	322	307	305	1.1	0.5

Source: Nirmal Bang Institutional Equities Research

Prices continue to gain strength in central region with healthy demand: Cement prices in central region strengthened ~4.5% YoY and ~1% MoM as demand in MP and UP continues to gain momentum. Housing demand is emanating in certain regions of UP, according to our channel check. With strong infrastructure demand in the region already in place, incremental demand from housing sector will help pricing in the state. Cement demand, which was subdued in MP in the recent past because of assembly elections and formation of the new government, is gaining momentum as the new government has given fresh impetus to infrastructure projects in the state.

Demand green shoots in northern region: Demand in northern region including Punjab and Delhi has witnessed green shoots in the recent past. Delhi's real estate demand is a mixed bag with an uptick in a few pockets. In Punjab, demand is healthy supported by infrastructure projects. Further, supply scarcity on lack of cement imports from Pakistan implies likely price stability in Punjab. Rajasthan demand is slowly picking up as the new government stabilises in the state, while early indications point towards a re-jig of projects announced by the previous state government.

Strong price trigger in southern region expectedly fails to keep pace, impacts demand: Our interaction with trade channels indicates that cement prices were weak, except in Bengaluru, in southern region after the sharp rise in February 2019. The pace of price gains of late, despite the continued demand-supply imbalance in the region, effectively led to demand waning. Further, with the mega Kaleshwaram lift irrigation project nearing its completion, bunching of supply will keep the despatches higher in Telangana. In Kerala, the rebuilding process after recent floods lacked the expected pace, thereby keeping the demand listless. The prices reversed MoM by ~5% except in Bengaluru. However, the pace of the jump in prices in February 2019 meant that YoY growth in prices was strong at 18.5%, despite the correction in March 2019.

Prices in western region remain mixed: Prices in Maharashtra gained further pace in March 2019 because of curtailed supply from southern region (from Karnataka in south Maharashtra and from Telangana to Vidharbha), effectively leading to relative supply paucity in Maharashtra region. Even in Mumbai, prices jumped 5% MoM without a real pick-up in demand. However, in Gujarat UTCCEM's taking over Binani Industries' assets implies that UTCCEM now caters to some pockets of north Gujarat cost effectively, leading to price weakness, according to our channel check. South Gujarat also is catered to aggressively by UTCCEM from its new assets, thereby keeping the prices under check. This has impacted the performance of relatively smaller companies like JK Lakshmi Cement. Although the demand is strong in Gujarat, new supply following the acquisition of Binani Industries' assets by UTCCEM is expected to keep the prices under pressure in the short term.

Eastern region pricing continues to be listless: Eastern region continues to be listless with 2% decline YoY and 1% MoM largely because of no major demand back-up. This is essentially because of a higher base in the region. Further, weakness in Odisha because of assembly elections in the state has impacted the pricing. The relatively stronger markets continue to be West Bengal and Jharkhand in the region.

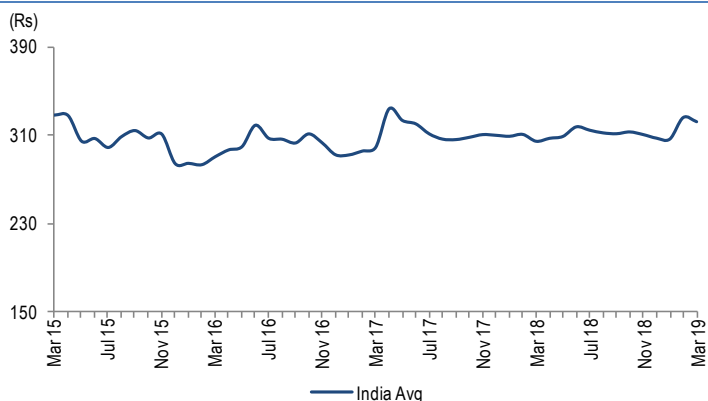
Outlook: Cement demand is expected to lose momentum in the medium term because of the forthcoming general elections in India, being supported only by existing projects due for completion and is expected to be listless unless political clarity emerges. The pace of strong demand growth, as indicated by the official data, will slow down and is likely to end with growth in lower teens. The demand from government projects including roads, irrigation, and low-cost housing will continue but incremental demand from new projects is unlikely, leading to a lull in demand in the interim phase. New supply addition announcements are only adding to the worries, as pricing power may get postponed further. We expect the performance of cement companies to be marginally better with the help of steady pricing and partial benefits of relative softening of costs in 4QFY19.

Exhibit 1: Monthly price movement across various cities (Rs/bag)

Region / city	March 2019	February 2019	March 2018	YoY Change (%)	MoM change (%)
Western	305	309	298	2.3	(1.3)
Mumbai	342	326	301	13.7	4.8
Ahmedabad	300	310	320	(6.3)	(3.2)
Surat	290	300	315	(7.9)	(3.3)
Nagpur	300	315	295	1.7	(4.8)
Nashik	300	300	270	11.1	-
Pune	300	305	290	3.4	(1.6)
Eastern	311	315	318	(2.0)	(1.2)
Kolkata	325	335	345	(5.8)	(3.0)
Raipur	245	250	255	(3.9)	(2.0)
Odisha	295	295	300	(1.7)	-
Bihar	380	380	370	2.7	-
Southern	365	379	308	18.5	(3.7)
Chennai	390	395	340	14.7	(1.3)
Hyderabad	315	335	260	21.2	(6.0)
Bengaluru	400	400	330	21.2	-
Vizag	322	342	267	20.6	(5.8)
Kochi	400	425	345	15.9	(5.9)
Northern	303	298	293	3.4	1.7
Delhi	300	295	285	5.3	1.7
Jaipur	290	280	270	7.4	3.6
Punjab	320	320	325	(1.5)	-
Central	320	318	306	4.5	0.8
Kanpur/Lucknow	350	335	315	11.1	4.5
Meerut	315	320	295	6.8	(1.6)
Indore	300	305	305	(1.6)	(1.6)
Bhopal	315	310	310	1.6	1.6
All India average	322	326	305	5.8	(1.2)

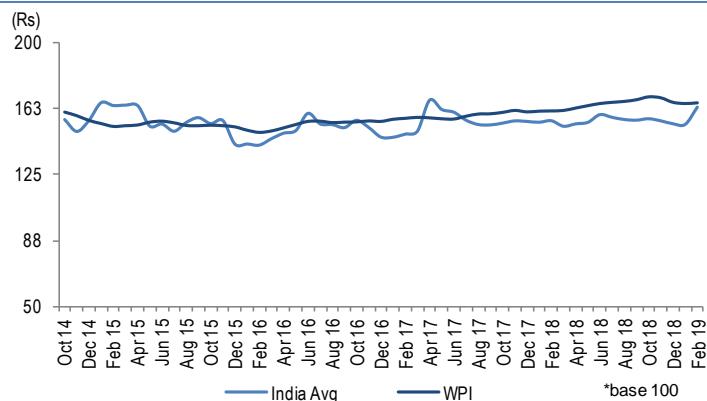
Source: Nirmal Bang Institutional Equities Research

Exhibit 2: Pan-India cement prices jump YoY driven by southern and western regions, decline MoM



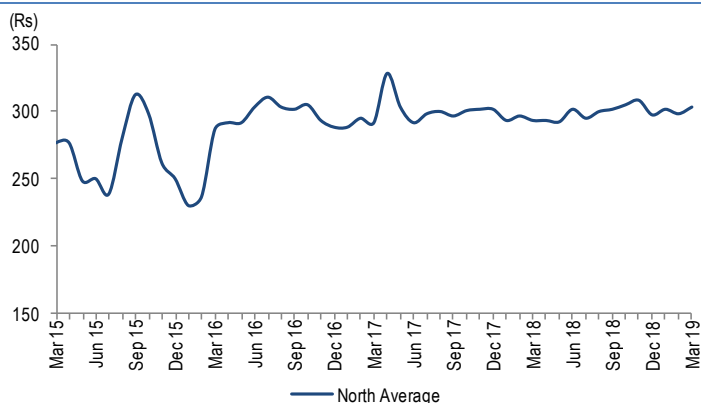
Source: Nirmal Bang Institutional Equities Research

Exhibit 3: Gap between India average cement price and Wholesale Price Index-based inflation narrows



Source: Nirmal Bang Institutional Equities Research

Exhibit 4: Price hike in northern region without demand support



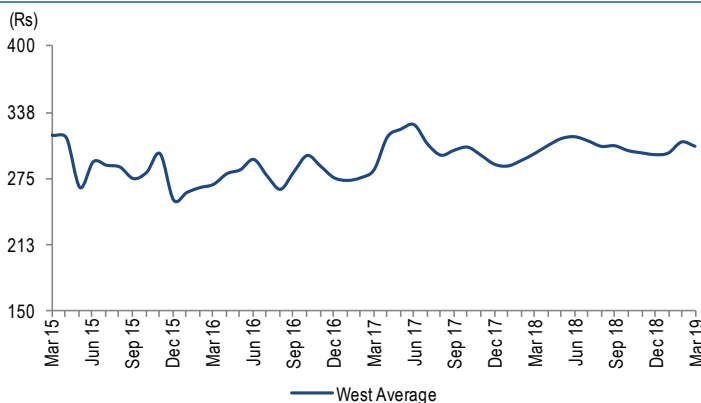
Source: Nirmal Bang Institutional Equities Research

Exhibit 5: Eastern region continues to remain listless



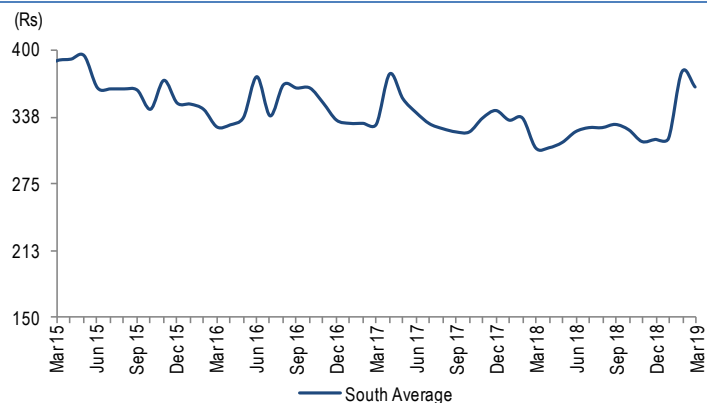
Source: Nirmal Bang Institutional Equities Research

Exhibit 6: Prices mixed in western region



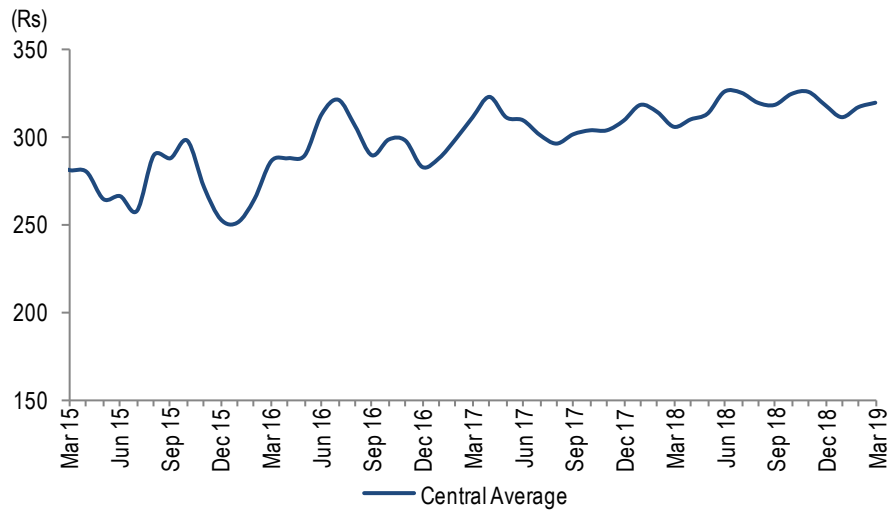
Source: Nirmal Bang Institutional Equities Research

Exhibit 7: Southern region fails to sustain the pace of price hikes



Source: Nirmal Bang Institutional Equities Research

Exhibit 8: Central region stays as the best cement market



Source: Nirmal Bang Institutional Equities Research

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