HD **Sluggish economic conditions soften the near-term outlook for Indian cement industry**

WC 2,655 words

PD 2 April 2014

SN Accord Fintech

SC HTACCF

LA English

LP

India, April 2 -- Cement is the glue that grips the concrete together, and is therefore critical for people's needs of housing as well as infrastructure development of any country such as bridges, roads, water treatment facilities, schools and hospitals. Indian cement industry has evolved significantly over the last two decades and today 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. The industry has transited itself into a more advanced one, aligning itself with the technological revolution, matching international standards. India the second largest producer of cement and housing sector is the biggest demand driver of industry, accounting for about 64% of the total country's consumption.

TD

Indian cement industry is highly organized with top 12 cement firms have around 70% share in the total domestic demand. However, India's per capita consumption of cement still remains substantially lower when compared with the world average. Cement industry is a freight intensive sector and transporting cement over long distances can prove to be expensive for industry players. Therefore, the industry gets divided into five main regions include south, north, west, east and the central region. Among these regions, Indian Southern region has the highest installed capacity, representing around one-third of the country's total installed cement capacity. On global level, industry is relatively insulated with low share in exports as well as imports. Industry PerformanceCement industry is highly correlated to the economic scenario as the demand for cement mainly depends on the level of development and the rate of growth of the economy. Indian cement consumption grew at a CAGR of 9.7 percent to 260 Million Tonnes (MT) during FY13 from 163.4 MT in FY08. Increasing infrastructure development and growing housing sector are the leading factor credited for increasing domestic cement demand. Some eminent industry side advantages like robust development on technological front, increasing presence of Tier II cement players and use of alternative fuels to lower production costs all have provided the much needed platform to boost the industry's growth. The presence of small and mid size players has been growing across all regions helping to lessen the market share of larger players. These tier II cement players have been constantly increasing their installed capacity in order to cater to increasing cement demand. Further, cement companies have started using alternate fuels, especially bio energy, which has reduced their production cost, besides proving effective in reducing emissions. Further, the government's move to boost the country's infrastructure has significantly contributed to the industry's growth. India's cement consumption is expected to be more than 450 MT per annum by FY20. With the focused growth and appropriate planning for sector, Indian cement sector has emerged as one of the most attractive sectors in the world. Over the past few years, industry has been receiving high foreign investment as well as private equity investment. Industry has also witnessed around seven M&A deals worth a total $3.3 billion since January 2013. While, during the period April 2000 to November 2013, cement and gypsum products sector in India has attracted foreign direct investments (FDI) worth $ 2,879.9 million. Cement industry, being highly sensitive to country's GDP growth is under pressure over the past two fiscal years owing to the prevailing economic slowdown. Indian economy's growth declined to a decade low at 4.5 percent in FY13 and 4.6 percent during the first three quarter of FY14. Indian cement consumption growth slowed down to 7 percent during FY13 from 10 percent average annual growth witnessed during the period FY08-FY12. Sluggish infrastructure development in the country as well as subdued demand for India's housing sector owing to the prevailing high interest rates as well as high inflation are the leading factors responsible for the declining domestic cement consumption. Amid lower cement offtake, industry players are operating at low capacity utilisation at around 75 percent, while in some regions it is not more than 60 percent. Furthermore, domestic players are continuously losing pricing power, while production costs continue to rise. So far this fiscal has proved worst in a decade for the industry in terms of growth. Snatch of negative factors is only getting tightened, impacting domestic cement industry to such an extent that major players either witnessed flat growth or negative growth in cement sales. Therefore, domestic cement consumption is likely to remain under pressure in the near term on account of sluggish demand. Cement can be produced through two basic processes - dry process and wet process. Dry process, being cost efficient, is widely used by manufactures representing around 97% of production capacity in India. Cement plants are mainly situated near limestone reserves as it is unviable for the manufacturer to transport raw material for long distances due to high logistic costs. Out of the seven lime stone reserves identified in the country, three are located in the Southern Region making it leading suppliers of cement in the country. Indian cement industry produces a variety of cement which includes Blended Cements, Ordinary Portland Cement (OPC) and Special cement include white and **oil** well cement. Blended cement accounts for around 75% of the domestic market, whereas OPC and special cements represent the remaining demand. During FY13, India has total 550 cement plants out of which 185 are large cement plants. Sluggish demand reducing capacities utilizationAt present, industry installed capacity stands at around 360 **million** tonnes. Capacity expansion increased at a CAGR of around 12 percent during the period FY08-FY13 whereas domestic cement consumption increased by CAGR of about 10 percent, forcing the manufactures to operate at low capacity. Amid expectation of strong growth in future, industry witnessed Rs 50,000 crore rapid expansions during 2007-2014 to nearly double cement capacity from 180 MT, fastest in domestic sectors' history. This rapid capacity expansion has increased high financial burden and is now proving a self-made trap for the cement makers. 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 cement demand. Demand for cement in India is cyclical and remain low during the monsoon session. However, during the current fiscal, cement demand in the country failed to pick up even in the post monsoon season as infrastructure and real estate sectors, major demand drivers for cement, are struggling with slowdown. During April-December 2013, cement production has remained subdued, increasing by only 3.7% from a year earlier. On the other hand, cement prices continued to remain under pressure owing to the weak demand, impacting margins of the industry players. Given the slow recovery in Indian economy and excess capacity in the industry, prices may remain soft in the near term. Rising costs squeeze profit marginsOver the past two years, shipment costs for industry has significantly increased as a result of a raise in freight rates by railways, high diesel prices and increasing dependence on expensive road transport due to a shortage of railway wagons. Industry is highly **energy** intensive as around 800-1000 Kcal of **energy** is required for the production of one kg clinker (cement). Further, around 30 percent of total expenses are being spent on power and **energy** needs of the plant. Thus, many large companies resort to captive power plants in order to reduce the power costs, as this source is economical and results in continual supply of power. Therefore, higher the captive power consumption of the **company**, the better it is for the **company**. Access and proximity to raw material (limestone) and consuming markets are also very important as it is extremely bulky commodity.**Coal** is the dominant fuel for the production of cement and acts as a strong driver towards efficiency. Around 0.22-0.25 tonne of **coal** is required in a typically dry process system for the production of one tonne clincker. Indian cement industry consumes about 10 **million** tonnes of **coal** annually. At present, Indian domestic **coal** demand is around 35 percent higher than domestic supply. Over the past couple of years, there has been a steep drop in the supply of linked **coal** to the cement industry from 70 percent in FY04 to almost 39 percent now, mainly due to diversion of **coal** to the power sector. Cement companies, therefore, have to resort to import **coal** from Indonesia, South Africa and Australia which works out to nearly 2 to 2.5 times higher than the domestic price or use of the alternate fuel like pet coke, lignite, etc. which also adds up significantly to the additional cost of production. However, over the past eight months global **coal** supplies has improved, leading to decline in the prices of international as well as domestic **coal**. Australian thermal **coal** monthly price has declined to $81.74 per metric ton, lowest since Nov 2009. The downward movement in **coal** prices is likely to have a positive impact on the margins of the cement companies. Industry SegmentsIndian cement industry can be divided into three segment viz; housing segment, infrastructure segment and commercial real estate. Among these segment, housing is the largest segment of the industry accounting for around 64% of the total cement demand. Commercial real estate and industrial represent around 19% share in the domestic cement consumption. Housing SegmentThe Housing segment represents a major portion of the total domestic demand for cement in India. Cement demand from rural housing is mainly driven by rising rural income (85%) and government-supported schemes (15%). Cement demand from this sector has been rising at a CAGR of around 10 percent over the past five years. Increasing number of households, growing urbanization and higher employment are primarily driving the demand for housing. Demand for affordable houses is growing in order to meet the demand for lower income group, while the rising income level of people are leading to higher demand for luxury products. However, at present the cement demand from housing sector is under pressure as prevailing high interest rates along with high inflation has been restricting people for financing new houses. Housing segment demand is likely to remain subdued amid prevailing high interest rates scenario. Infrastructure and Commercial Real Estate SegmentsInfrastructure segment accounts for around 17% of the total cement demand in India. Over the past one and half decade, the demand of cement for infrastructure sector grew significantly as brisk growth rate of Indian economy achieved since 2000, has given a tremendous fillip to the infrastructure development in the country. The increase in industrialization activities by public and private companies has resulted in increased demand for updated quality building material including cement. Furthermore, high economy's growth witnessed during past period also led to increase in demand for commercial real estate segment, hotels, multiplexes and retail space as well as municipal facilities including hospitals, and schools. Over the past decade, increasing number of multinational companies and the growth of the services sector has augmented the demand for office space in India, whereas growth in tourism, including both business and leisure travel, has boosted the construction of hotels in the country. However, currently, infrastructure and commercial real estate sectors are struggling with slowdown due to prevailing economic downturn. The factors such as slower government spending on infrastructure development amid mounting concerns over high fiscal deficit and lethargic services sector demand leading to sluggish expansion of hotel and multiplexes are directly impacting the cement demand. Besides, slow recovery in the capital expenditure cycle by private firms and uncertainty about the new government after general election in May 2014 is also compelling companies defer their investment plans. Therefore, demand of cement from these sectors is likely to remain sluggish in coming future. Issues and ConcernsHighly Taxed Industry: Although cement is a crucial product for the development of country's infrastructure, it is one of the highly taxed commodities that has ex-factory price at 60%, which translates even more than one levied on luxury goods. Presently, industry attracts multiple rates of excise duty, depending on maximum retail price (MRP) and nature of packing, which further varies according to the producer (large or small and white cement plants) and quantum of clearance. The overall rate of tax on cement stands around 30%, which is far higher than around 19% in **China** and other Asia region countries. Prevailing economic slowdown: Demand of cement in India is cyclical and barring short term disruptions it grows entirely in tandem with economic growth. Cement demand is mainly derived from the housing real estate and infrastructure sectors, which are closely linked to overall economy's growth. Sluggish domestic demand due to economic downturn coupled with high interest rates and inflation are impacting real estate and infrastructure sectors which in turn put pressure on cement demand. Furthermore, cement plant, being a capital intensive unit, higher interest cost acts as a disincentive for fresh investment for the industry. Therefore, prevailing economic slowdown has become an issue for Indian cement industry.   Excess cement capacity: Currently, India's cement production capacity stands at around 370 MT, which is much higher than around 270 MT cement demand. The industry has created the capacity on the back of government's projection of potential cement demand arising out of the thrust given for infrastructure development in the country and the allocation of funds earmarked for the purpose. Such huge investment has increased the financial burden on industry players. Conversely, cement prices continued to remain low because of weak demand, impacting industry margins. To add the woes, one fourth of the industry's capacity is presently remainly unutilized due to sluggish demand. OutlookThe cement industry, a part of the manufacturing sector, plays a crucial role in the growth and development of the nation. As cement demand is derived from housing, infrastructure and commercial real estate & industrial sectors, the performance of the cement industry is therefore largely dependent on overall economic growth of the country. However, the slowdown in domestic demand, high inflation, slower government spending on concerns over ballooning fiscal deficit coupled with weaknesses in the global economy have resulted in a slowdown in India's growth, impacting domestic cement demand. Furthermore, rising raw material costs, excess cement capacity, high tax burden have become key concerns for the industry. In the near term, the growth of Indian cement industry is likely to remain under pressure as growth in economy is still not picking up. However, the medium to long term outlook looks bright for industry given the huge untapped housing demand and increasing infrastructure development in the country. Also, India's per capita cement consumption is still abysmally low at around 185kg per annum as compared to global average of nearly 300kg per capita, reflecting a strong growth opportunity in the domestic market. The focus of the Government on strengthening infrastructure, promotion of low-cost affordable housing and rising per capita incomes are likely to augur well for the cement industry. With the increasing industrial activities along with the development of various Special Economic Zones (SEZs) across India, there is an uninterrupted demand for cement. Further, in order to boost infrastructure development, the Government plans to increase investment in infrastructure to $1 trillion during the 12th Five Year Plan (2012-17).

Published by HT Syndication with permission from Accord Fintech.

CT For any query with respect to this article or any other content requirement, please contact Editor at htsyndication@hindustantimes.com

IN i242 : Cement/Ready-mix Concrete | ihotel : Hotel Construction | i501 : Building Construction | ibuildpr : Building Materials/Products | iconst : Construction | icre : Real Estate/Construction

RE india : India | austr : Australia | apacz : Asia Pacific | asiaz : Asia | ausnz : Australia/Oceania | bric : BRIC Countries | devgcoz : Emerging Market Countries | dvpcoz : Developing Economies | indsubz : Indian Subcontinent | sasiaz : Southern Asia

PUB Accord Fintech

AN Document HTACCF0020140402ea420007t

