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Cement prices — subdued amid rising costs

All-India cement prices declined by Rs 3/bag mom to Rs 328/bag in June, 2018 giving away the modest gains seen in the previous two months. We note that cement prices increased by Rs 4-5/bag in months of April and May, 2018. The prices are much lower than Rs 343/bag seen last year in June, 2017 even though costs have risen. In June, 2018, prices declined in South (-Rs 10/bag mom) followed by West (-Rs 4/bag mom) while North and East remained largely flat. Our checks indicated a price increase of Rs 5/bag mom in the Central region.

Cost challenges to rise in FY2019e

The cost environment remains challenging due to rising pet-coke prices and diesel prices. Additionally, the weakening INR/US\$ will add to the rising cost pressure of cement companies — we estimate that close to 35% of the costs of cement companies is impacted due to forex movement. The spot pet-coke price is 18% higher than FY2018 prices (in INR terms) while diesel prices are 17% higher. Slag prices remain high from strong sales of blended cement in many regional markets.

Lower spreads to result in weak Q1FY19 earnings

The spreads have drifted down since September, 2017 and continue to remain weak in the absence of price improvements and rising fuel costs, of both pet-coke and coal. Accordingly, Indian cement companies reported a strong Ebitda/ton in 1HFY18 (Rs 950/ton average) and lower in 2HFY18 (Rs 794/ton). We expect Q1FY19 to be no better due to weak spreads and to be additionally impacted by rising freight costs.

Cautious stance on the sector

We maintain our cautious stance on the cement sector on expensive valuations and on expectations of moderate improvement in earnings over the next two years. The cost headwinds on the back of rising fuel costs, weakening INR/US\$ rate necessitate a sharp improvement in industry utilisation for meaningful earnings improvement. However, we believe close to 70 mtpa of new capacities over the next three years will keep industry utilisations low (<70%).

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