

June 28, 2022

Passing through bumpy roads; time to stick with leaders

The cement sector is likely to witness a glut of new supplies over the next three to four years (i.e. at 7.2% CAGR) based on the recent capex plan announced by major cement companies. Assuming some delays, we still expect supply CAGR of 6-6.5% vs. historical average of 4.4%. This would lead to fresh rounds of consolidation especially in the mid and small sized cement players having high cost structure/bloated b/s. The near-term cost headwinds have already pressurised margins as player are unable to pass on the cost pressure due to moderation in demand in the wake of higher inflation. This has led to cement sector underperforming broader markets. While long-term demand is expected to stay healthy, we believe, the recent stock price correction offers a good entry point to accumulate quality companies having healthy b/s and sustained long-term growth visibility despite near-term challenges.

Increased competitive intensity to keep utilisations under check

Going by the recent capex announcement along with their timelines made by major cement companies, we expect industry capacity growth to accelerate to over 7% over next three years (refer exhibit-1). Assuming some delays/deferments, capacity is still likely to grow at CAGR of 6-6.5% during the same period. Historically, the industry has witnessed capacity CAGR of 4-4.5% over the past 10 years (i.e. from ~350 MT in FY12 to over ~540 MT in FY22). With five major players (controlling ~49% capacity share) announcing aggressive capex plans, the industry capacity utilisation would be unlikely to improve despite better demand outlook. This would lead to fresh rounds of consolidation in the Industry especially in the mid and small sized cement having high cost structure/bloated b/s in our view.

Inflationary pressure on margins to be felt in medium term

Compared to Q4 average, prices of international coal, petcoke are up 40%, 45%, respectively. In the absence of major price hike due to moderate demand despite being the peak construction season, input cost inflation is likely to remain a key concern for the sector in the near term. The recent attempts for prices increases in April 2022 saw partial rollbacks in May 2022. Now, the beginning of the monsoon would limit the ability of cement players to hike cement prices over the next three to four months. This, in our view, should be an incremental headwind of ~₹ 300/t on margins for our covered companies.

Remain selective, prefer companies with efficient cost structure, focused towards driving higher CF/total capex

Given the cement sector's healthy long-term growth potential, which is currently being reflected in the low per capita consumption (i.e. at ~250/kg vs. global average of ~550/kg per capita), we expect demand to grow at a CAGR of 6-6.5% over the next four to five years. This will be driven by good monsoon, higher farm realisations and the government's focus on infrastructure, especially affordable housing and road construction, in the run-up to general elections in India in 2024. On the cost front, the recent measures by the government (like ban on steel exports, excise duty cut on diesel) would help in moderating the inflationary pressure. However, major cost benefit for cement companies would accrue only after structural downturn in the petcoke/coal prices that are still trading at elevated levels. Hence, we remain selective and prefer companies, which are not only cost efficient but also prudent in generating higher cash flows to total capex. The recent stock price correction offers a good entry point to accumulate these companies having healthy b/s, pan India presence and sustained long term revenue and earnings growth prospects. **Our key top picks are UltraTech and Shree Cement.**

Top Picks in Cement Space

Company	CMP (₹)	Rating (₹)		Target (₹)		Upside (%)
		Old	New	Old	New	
UltraTech	5560	BUY	BUY	8000	7500	35
Shree	19100	HOLD	BUY	24300	24300	27

Cement stocks have been underperforming broader markets broadly on the back of:

- Aggressive capex announcement by major players in bid to retain market share
- Inflationary situation led by sharp rise in the power and fuel cost
- Inability of players to fully pass on the cost pressure

Key risks to our call

- Lower than anticipated sales volume growth over FY22-24E
- Prolonged inflationary situation

Research Analysts

Rashesh Shah
rashes.shah@icicisecurities.com

Cement capacity to grow at 7.2% CAGR over next three years vs. long term average of 4.4% CAGR

Exhibit 1: Player wise capacity trends (FY12-25E)

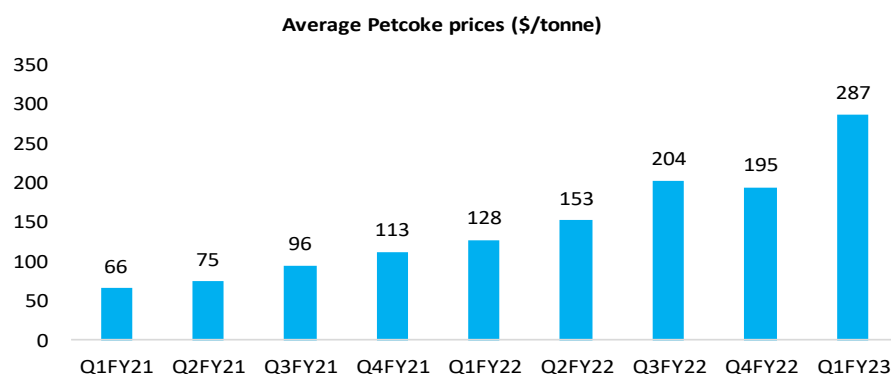
Capacity (MT)	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	FY22	10Year CAGR (%)	FY23E	FY24E	FY25E	3Year CAGR (%)
Ultratech	48.1	50.2	53.1	59.3	63.2	66.3	80.6	109.4	111.4	111.4	114.6	9.1%	130.9	141.9	153.5	10.2%
Shree	13.5	13.5	17.5	22.1	25.6	29.3	34.9	37.9	43.4	43.4	46.4	13.1%	49.4	52.9	59.9	8.9%
Ambuja	28.0	28.0	28.0	28.8	29.7	29.7	29.7	29.7	29.7	29.7	31.5	1.2%	33.0	38.5	45.2	12.8%
ACC	29.0	30.5	30.5	31.0	31.0	31.0	33.1	33.1	33.1	33.1	34.5	1.8%	37.1	39.3	50.3	13.4%
Dalmia	18.9	18.9	22.8	24.9	24.9	24.9	24.9	26.5	27.3	30.6	35.9	6.6%	40.9	48.5	53.5	14.2%
Nuvoco	11.0	11.0	11.0	13.3	13.3	13.3	13.3	14.1	23.5	25.0	25.0	8.5%	25.0	25.0	25.0	0.0%
JSW Cement	0.6	3.6	6.0	6.0	6.4	7.6	11.2	12.6	14.0	14.0	16.4	39.2%	19.4	21.8	25.0	15.1%
Birla Corp	6.3	7.0	8.5	9.8	9.8	15.4	15.4	15.4	15.4	15.4	19.3	11.8%	20.7	20.7	23.5	6.8%
Ramco	12.5	14.5	15.5	15.5	16.5	16.5	16.5	16.7	18.3	19.2	20.2	4.9%	20.2	20.2	20.2	0.0%
JK Cement	7.5	7.5	7.5	10.5	10.5	10.5	10.5	10.5	14.0	14.7	14.7	7.0%	14.7	18.7	18.7	8.4%
India Cements	15.6	15.6	15.6	15.6	15.6	15.6	15.6	15.6	15.6	15.6	15.6	0.0%	15.6	18.1	18.1	5.1%
JK Lakshmi	5.9	5.9	7.7	8.2	8.6	10.9	10.9	12.5	13.3	13.3	13.9	8.9%	13.9	16.4	16.4	5.7%
Chettinad	15.5	15.5	15.5	15.5	15.5	15.5	15.5	15.5	15.5	15.5	15.5	0.0%	15.5	15.5	15.5	0.0%
Wonder Cement	11.0	11.0	11.0	11.0	11.0	11.0	11.0	11.0	11.0	13.0	13.0	1.7%	13.0	13.0	13.0	0.0%
Orient	5.0	5.0	5.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	4.8%	10.5	10.5	10.5	9.5%
Panna	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	0.0%	10.0	10.0	10.0	0.0%
MyHome Ind	8.0	8.5	8.5	8.5	8.5	10.1	10.1	10.1	10.1	10.1	10.1	2.4%	10.1	10.1	10.1	0.0%
Sagar	2.7	2.7	2.7	2.7	2.9	4.0	4.3	5.8	5.8	5.8	8.3	11.9%	8.3	11.0	11.0	9.9%
Others	102.0	113.3	116.7	116.5	125.2	130.6	118.6	101.9	105.7	93.5	87.4	-1.5%	86.1	88.9	85.6	-0.7%
Total Capacity	351	372	393	417	436	460	474	496	525	521	540	4.4%	574	621	665	7.2%

Source: Company, ICICI Direct Research

Impact of elevated fuel prices to get reflected from Q1FY23

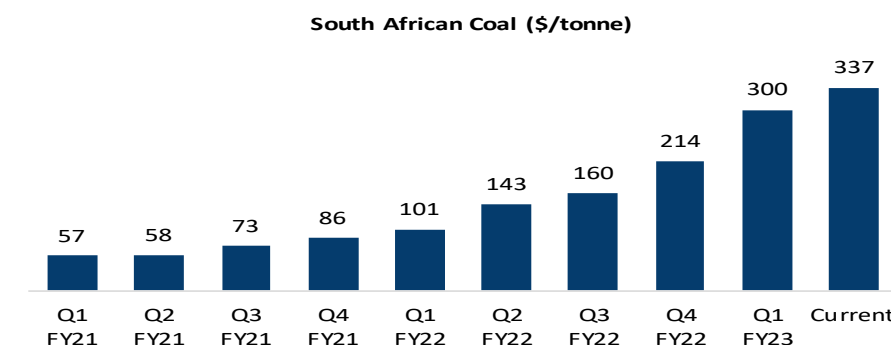
Compared to Q4 average, prices of international coal, petcoke are up 40%, 45%, respectively. In the absence of major price hike due to moderate demand despite being the peak construction season, input cost inflation is likely to remain a key concern for the sector in the near term.

Exhibit 2: Petcoke price trend



Source: Company, ICICI Direct Research

Exhibit 3: International coal prices



Source: Company, ICICI Direct Research

Pet coke prices have spiked again in Q1FY23, So far, prices on an average are up ~45% QoQ and ~120% YoY

Prices of imported coal have also surged by 39% from the Q4FY22 average. Now, on an average, they are up 198% YoY

However, in our view, the current price levels for coal and petcoke are unsustainable. Hence, we expect a downward correction in the medium term

Top bets in Cement Coverage Universe

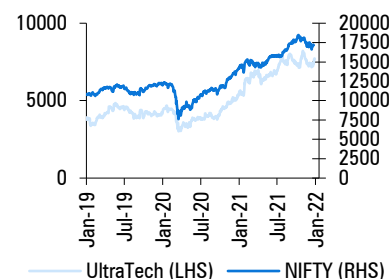
UltraTech Cement (ULTCEM)

UltraTech is the largest cement manufacturer in India with a domestic capacity of 114.5 MT. It has grown through organic and inorganic routes and added around ~30 MT of capacity in the last three years. It has shown its capability to successfully integrate the acquired assets and ramped-up its utilisations in a profitable manner.

- The board has approved cement capacity expansion of 22.6 MT at a capex of ~₹ 12,900 crore (US\$76/t) which the company expects to complete by FY25. This will take its total India grey cement capacity to ~154 MT implying 10.2% CAGR during the next three years

These new capacities are being added at a much cheaper rate compared to replacement value (i.e. EV/tonne of \$76/tonne vs. industry average of \$125/130/tonne). This clearly shows efficiency in the capex allocation. Further, with strong b/s, the company is best placed to ride on competition and maintain return ratios vs. its peers. We continue to maintain **BUY** rating with a target price of ₹ 7,500/share (i.e. at 15.5x FY24E EV/EBITDA).

Price Chart



Particulars

Particulars	Amount
Mcap	₹ 160446 cror
Debt (FY22)	₹ 9891 cror
Cash & Invest (FY22)	₹ 155 cror
EV	₹ 170182 cror
52 week H/L	₹8269/₹519

Exhibit 4: Financial summary

Key Financials	FY19	FY20	FY21	FY22	3 Year CAGR (%)	FY23E	FY24E	2 Year CAGR (%)
Net Sales (₹ crore)	39933	40634	43188	50663	8.3	61173	65976	14.1
EBITDA (₹ crore)	7076	8652	10964	10936	15.6	10896	13677	11.8
EBITDA (%)	17.7	21.3	25.4	21.6		17.8	20.7	
Adjusted PAT (₹ crore)	2530	4448	5506	7067	40.8	5688	7593	3.7
EPS (₹)	87.7	154.1	190.8	244.9		197.1	263.1	
EV/EBITDA	24.6	19.9	15.2	14.9		14.6	11.4	
EV/t (\$)	223	221	182	178		174	170	
RoNW (%)	7.6	11.6	12.7	14.4		10.6	12.7	
RoCE (%)	9.0	11.4	14.7	14.2		13.6	16.6	

Source: Company, ICICI Direct Research

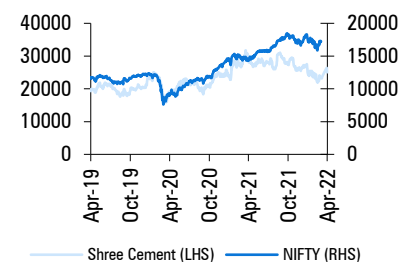
Shree Cement (SHRCEM)

Shree is the third largest cement group in India with domestic cement capacity of 46.4 MT as of FY22. In the past four years, it has diversified itself from being 100% North player to the player with capacities now in Rajasthan, Bihar, Chhattisgarh, Haryana, UP, Karnataka and Odisha.

- Proximity to end user market, use of split grinding units and power capacity of 742 MW (Including 211 MW WHRS) makes it the most efficient player in the industry

With commissioning of 3 MT grinding unit in Maharashtra, domestic capacity has reached 46.4 MT in FY22. Other new capex includes 1) setting up of new integrated unit with 3.5 MT GU and 3.8 MT clinker unit in Rajasthan by Q4FY24E at a capex of \$135/t 2) 3 MT grinding unit in West Bengal by Q4FY23E at a capex of \$34/t, 3) 106 MW solar power at capex of ₹ 4.7crore per megawatt (MW). The entire capex of ₹ 4750 crore till FY24E will be funded via internal accruals. Post recent price corrections, we now turn positive on the company and upgrade our rating from HOLD to **BUY** with an unchanged TP of ₹ 24300/share (i.e. 19x FY24E EV/EBITDA).

Price Chart



Particulars

Particular	Amount
Mcap	₹ 69028 crore
Debt (FY22)	₹ 2345 crore
Cash & equivalent(FY2)	₹ 3603 crore
EV	₹ 67769 crore
52 week H/L	₹ 31400 / 17900

Exhibit 5: Financial summary

Key Financials	FY19	FY20	FY21	FY22	3 Year CAGR (%)	FY23E	FY24E	2 Year CAGR (%)
Net Sales	11722	11904	12653	14306	6.9	16530	18632	14.1
EBITDA	2653	3675	3979	3648	11.2	3624	4410	9.9
EBITDA (%)	22.6	30.9	31.4	25.5		21.9	23.7	
PAT	1108	1570	2312	2376	29.0	2054	2566	3.9
EPS (₹)	318	435	641	659		569	711	
EV/EBITDA	27.2	18.8	17.0	18.6		18.3	14.8	
EV/Tonne (\$)	239	201	198	202		163	160	
RoNW	11.5	12.1	15.2	13.8		10.9	12.2	
RoCE	11.5	13.8	18.2	16.1		14.0	15.8	

Source: Company, ICICI Direct Research

Ranking of cement companies on various parameters

Exhibit 6: Shree Cement remains low cost producer among large players

Total cost/tonne	FY17	FY18	FY19	FY20	FY21	FY22
Sagar Cement	3,196	3,345	3,216	3,161	3,074	3,667
Shree Cement	2,949	3,264	3,507	3,300	3,231	3,846
Orient Cement	3,057	3,336	3,453	3,515	3,512	3,895
Heidelberg ^	3,215	3,286	3,369	3,490	3,589	3,899
Ambuja ^	3,564	3,708	3,915	3,965	3,856	3,981
JK Laxmi Cement	3,202	3,533	3,587	3,670	3,620	4,007
Ramco	3,322	3,551	3,679	3,786	3,732	4,226
ACC ^	4,138	4,337	4,495	4,583	4,479	4,556
JK Cement	3,871	4,097	4,235	4,380	4,136	4,559
UltraTech Cement	4,802	4,802	4,802	4,802	4,802	4,802
Total	3913	4078	4215	4234	4204	4413

Source: Company, ICICI Direct Research

Exhibit 7: Shree cement & UltraTech both generate EBITDA of over ₹ 1200/t in FY22

EBITDA/Tonne	FY17	FY18	FY19	FY20	FY21	FY22
Shree Cement	1,220	1,095	1,026	1,473	1,482	1,316
UltraTech Cement	1,015	986	875	1,107	1,328	1,226
Ambuja ^	780	845	782	895	1,170	1,187
Ramco	1,409	1,181	949	1,024	1,553	1,155
JK Cement	877	809	822	1,209	1,301	1,082
Orient Cement	321	531	488	660	1,091	1,079
ACC ^	544	594	535	748	923	1,038
Heidelberg ^	556	720	938	1,096	1,118	910
Sagar Cements	501	571	450	592	1,268	765
JK Laxmi Cement	460	484	429	732	795	757
Total	898	880	809	1,048	1,255	1,158

Source: Company, ICICI Direct Research

Exhibit 8: UltraTech, Shree both occupy dominant position in terms of capacity

Capacity	FY17	FY18	FY19	FY20	FY21	FY22
UltraTech Cement	66.3	80.6	109.4	111.4	111.4	114.6
Shree Cement	27.5	31.9	37.9	43.4	43.4	46.4
ACC ^	32.5	33.4	33.4	33.1	33.1	34.5
Ambuja ^	29.7	29.7	29.7	29.7	29.7	31.5
Ramco	16.5	16.7	16.7	18.3	19.4	19.4
JK Cement	10.5	10.5	10.5	14.0	14.3	14.7
JK Laxmi Cement	9.9	10.9	11.2	11.7	11.7	11.7
Sagar Cement	4.1	4.4	5.3	5.8	5.8	8.3
Heidelberg ^	5.4	5.4	5.4	5.4	5.4	5.4
Mangalam Cement	3.6	4.0	4.0	4.0	4.0	4.0
Total	220	243	279	292	294	306

Source: Company, ICICI Direct Research

RATING RATIONALE

ICICI Direct endeavors to provide objective opinions and recommendations. ICICI Direct assigns ratings to its stocks according to their notional target price vs. current market price and then categorizes them as Buy, Hold, Reduce and Sell. The performance horizon is two years unless specified and the notional target price is defined as the analysts' valuation for a stock

Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



Pankaj Pandey

Head – Research

pankaj.pandey@icicisecurities.com

**ICICI Direct Research Desk,
ICICI Securities Limited,
1st Floor, Akruiti Trade Centre,
Road No 7, MIDC,
Andheri (East)
Mumbai – 400 093
research@icicidirect.com**

ANALYST CERTIFICATION

I/We Rashesh Shah CA, Deboto Sinha MBA, Research Analysts, authors and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report. It is also confirmed that above mentioned Analysts of this report have not received any compensation from the companies mentioned in the report in the preceding twelve months and do not serve as an officer, director or employee of the companies mentioned in the report.

Terms & conditions and other disclosures:

ICICI Securities Limited (ICICI Securities) is a full-service, integrated investment banking and is, inter alia, engaged in the business of stock broking and distribution of financial products.

ICICI Securities is Sebi registered stock broker, merchant banker, investment adviser, portfolio manager and Research Analyst. ICICI Securities is registered with Insurance Regulatory Development Authority of India Limited (IRDAI) as a composite corporate agent and with PFRDA as a Point of Presence. ICICI Securities Limited Research Analyst SEBI Registration Number – INH000000990. ICICI Securities Limited SEBI Registration is INZ000183631 for stock broker. ICICI Securities is a subsidiary of ICICI Bank which is India's largest private sector bank and has its various subsidiaries engaged in businesses of housing finance, asset management, life insurance, general insurance, venture capital fund management, etc. ("associates"), the details in respect of which are available on www.icicibank.com.

ICICI Securities is one of the leading merchant bankers/ underwriters of securities and participate in virtually all securities trading markets in India. We and our associates might have investment banking and other business relationship with a significant percentage of companies covered by our Investment Research Department. ICICI Securities and its analysts, persons reporting to analysts and their relatives are generally prohibited from maintaining a financial interest in the securities or derivatives of any companies that the analysts cover.

Recommendation in reports based on technical and derivative analysis centre on studying charts of a stock's price movement, outstanding positions, trading volume etc as opposed to focusing on a company's fundamentals and, as such, may not match with the recommendation in fundamental reports. Investors may visit icidirect.com to view the Fundamental and Technical Research Reports.

Our proprietary trading and investment businesses may make investment decisions that are inconsistent with the recommendations expressed herein.

ICICI Securities Limited has two independent equity research groups: Institutional Research and Retail Research. This report has been prepared by the Retail Research. The views and opinions expressed in this document may or may not match or may be contrary with the views, estimates, rating, and target price of the Institutional Research.

The information and opinions in this report have been prepared by ICICI Securities and are subject to change without any notice. The report and information contained herein is strictly confidential and meant solely for the selected recipient and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent of ICICI Securities. While we would endeavour to update the information herein on a reasonable basis, ICICI Securities is under no obligation to update or keep the information current. Also, there may be regulatory, compliance or other reasons that may prevent ICICI Securities from doing so. Non-rated securities indicate that rating on a particular security has been suspended temporarily and such suspension is in compliance with applicable regulations and/or ICICI Securities policies, in circumstances where ICICI Securities might be acting in an advisory capacity to this company, or in certain other circumstances.

This report is based on information obtained from public sources and sources believed to be reliable, but no independent verification has been made nor is its accuracy or completeness guaranteed. This report and information herein is solely for informational purpose and shall not be used or considered as an offer document or solicitation of offer to buy or sell or subscribe for securities or other financial instruments. Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. ICICI Securities will not treat recipients as customers by virtue of their receiving this report. Nothing in this report constitutes investment, legal, accounting and tax advice or a representation that any investment or strategy is suitable or appropriate to your specific circumstances. The securities discussed and opinions expressed in this report may not be suitable for all investors, who must make their own investment decisions, based on their own investment objectives, financial positions and needs of specific recipient. This may not be taken in substitution for the exercise of independent judgment by any recipient. The recipient should independently evaluate the investment risks. The value and return on investment may vary because of changes in interest rates, foreign exchange rates or any other reason. ICICI Securities accepts no liabilities whatsoever for any loss or damage of any kind arising out of the use of this report. Past performance is not necessarily a guide to future performance. Investors are advised to see Risk Disclosure Document to understand the risks associated before investing in the securities markets. Actual results may differ materially from those set forth in projections. Forward-looking statements are not predictions and may be subject to change without notice.

ICICI Securities or its associates might have managed or co-managed public offering of securities for the subject company or might have been mandated by the subject company for any other assignment in the past twelve months.

ICICI Securities or its associates might have received any compensation from the companies mentioned in the report during the period preceding twelve months from the date of this report for services in respect of managing or co-managing public offerings, corporate finance, investment banking or merchant banking, brokerage services or other advisory service in a merger or specific transaction.

ICICI Securities or its associates might have received any compensation for products or services other than investment banking or merchant banking or brokerage services from the companies mentioned in the report in the past twelve months.

ICICI Securities encourages independence in research report preparation and strives to minimize conflict in preparation of research report. ICICI Securities or its associates or its analysts did not receive any compensation or other benefits from the companies mentioned in the report or third party in connection with preparation of the research report. Accordingly, neither ICICI Securities nor Research Analysts and their relatives have any material conflict of interest at the time of publication of this report.

Compensation of our Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions.

ICICI Securities or its subsidiaries collectively or Research Analysts or their relatives do not own 1% or more of the equity securities of the Company mentioned in the report as of the last day of the month preceding the publication of the research report.

Since associates of ICICI Securities and ICICI Securities as a entity are engaged in various financial service businesses, they might have financial interests or actual/ beneficial ownership of one percent or more or other material conflict of interest various companies including the subject company/companies mentioned in this report.

ICICI Securities may have issued other reports that are inconsistent with and reach different conclusion from the information presented in this report.

Neither the Research Analysts nor ICICI Securities have been engaged in market making activity for the companies mentioned in the report.

We submit that no material disciplinary action has been taken on ICICI Securities by any Regulatory Authority impacting Equity Research Analysis activities.

This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject ICICI Securities and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.