

6 January 2009

## India Cement Sector

*Downhill slide to continue, trough in FY10*

Underweight

Nifty/Sensex: 3047/9958



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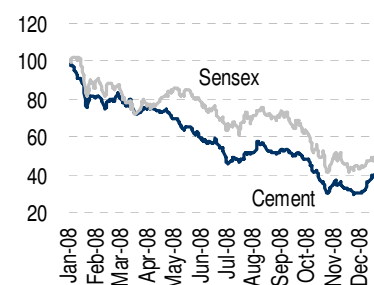
- **Underweight.** We initiate coverage on India's cement sector, with an Underweight. Massive capacity expansion, slumping demand and higher costs have pushed the sector into a downcycle, and we expect it to hit bottom by FY10.
- **Pricing power to weaken further.** We expect the 115m tons of capacity addition over the next three years to slice utilization to 74% by FY11, the lowest since FY95. This should also impact cement prices, which we expect to fall 10-15% across India over FY10-11, with the South and North zones hit the most.
- **Cost pressures to ease.** The softening in international coal prices is expected to lower the coal costs of cement companies by ~17% in FY10, post the impact of rupee depreciation. We, however, expect the reduced linkages and softening in cement prices to eat into the cost savings.
- **Demand slowdown ahead.** Over FY08-FY10, we expect a 7.7% demand CAGR (from 10% over FY05-08), based on cement-to-GDP co-relation of 1x. The slowdown in real estate (60% of demand) will limit any major upside. We expect a revival (8.5%) in FY11 on the back of lower interest rates and drop in realty prices.
- **Initiations.** We initiate coverage on six companies (~80% of the cement sector market cap). We have Sell ratings on ACC (TP: Rs410), Ambuja (TP: Rs53), UltraTech (TP: Rs354) and India Cements (TP: Rs82); Hold ratings on Grasim (TP: Rs1,305) and Shree (TP: Rs561).

### India cement sector – Valuation matrix

Key Data	ACC	Ambuja	Grasim	UltraTech	India	Shree
Rating	Sell	Sell	Hold	Sell	Sell	Hold
Price (Rs)	494	69	1,212	389	103	473
Target Price (Rs)	410	53	1,305	354	82	561
Difference (%)	(17.0)	(23.4)	7.7	(9.1)	(20.3)	18.7
Market Cap (US\$bn)	1.9	2.2	2.5	1.1	0.6	0.3
PE- FY10 (x)	12.0	13.3	6.5	8.0	6.2	4.2
EV/EBITDA- FY10 (x)	6.7	7.3	5.9	5.3	4.1	2.9
EPS CAGR FY08-11 (%)	(23.6)	(20.5)	(19.0)	(23.2)	(24.7)	4.1
EBITDA CAGR FY08-11 (%)	(17.5)	(16.0)	(12.0)	(14.2)	(14.3)	(12.0)
Target EV/ ton (USD)- FY10	59	86	65	62	53	48
Target EV/EBITDA- FY10 (x)	5.5	5.5	4.0	5.0	3.5	3.3

Source: Anand Rathi Research

### Sensex vs Cement Majors



Source: Anand Rathi Research

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