

Cement Sector

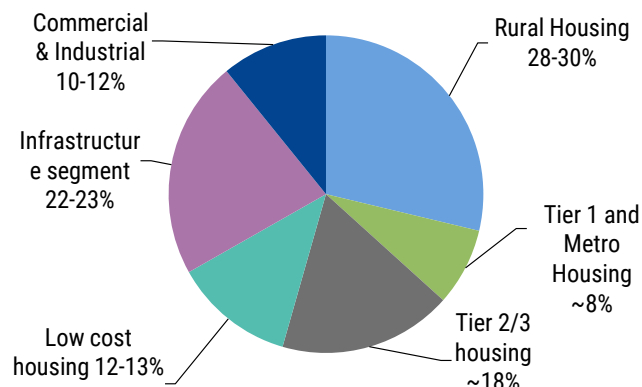
We have a positive stance on the cement sector reflected in our ownership of several large & mid cap cement stocks in our portfolios. We believe cement sector is a good proxy to play impending upcycle in the economy and revival in the real estate sector. Our positive view is based on the expected upturn in the cement cycle led by improving demand supply balance, better pricing environment with increasing industry consolidation and rising utilization levels.

Cement demand is expected to outpace supply by growing at CAGR c7% over FY20-23e period while capacity additions are expected to grow at CAGR c4% over the same period.

We expect the government's focus on housing (particularly affordable housing), infrastructure push and strong revival in overall real estate sector should augur well for strong growth in cement demand going forward. Difficulty and high cost of adding new cement capacity further improves the attractiveness of existing cement businesses.

Housing Sector - Almost after a decade we are seeing signs of revival in the real estate sector which is the biggest driver of cement demand and is estimated to account for about 2/3rd of the total demand. Housing activity has been robust in rural and semiurban areas driven by higher disposable incomes, rising aspirations and government sponsored schemes on affordable housing. Lower home loan rates, improving affordability and supportive state & central government policies have given fillip to housing demand in Metros/ Cities as well.

Chart1: Cement demand drivers FY 2020



Source: JM Financial Research.

Infrastructure - Building of infrastructures such as roads, ports, bridges, dams/irrigation projects, urban transportation (metros), airports etc. is the other big demand driver for cement. As the reform measures announced by the government start showing an impact on execution of existing and new infrastructure projects; cement demand will likely get another strong boost going ahead.

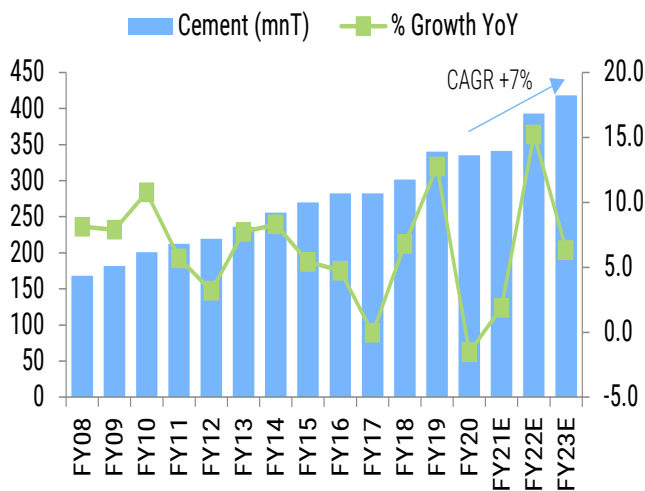
We believe that the companies in the sector will be able to mitigate margin pressures coming from rising raw material costs and freight costs by higher demand growth, their ability to pass on cost increases to the customers aided by better pricing discipline and by undertaking cost efficiency programs.

The cost of setting up new green-field cement capacity has increased significantly with land acquisition issues and access to raw material resources becoming difficult. This adds to the attractiveness of existing cement businesses from an investment perspective. We therefore expect select cement stocks to continue to outperform in the medium to long term.

Key Risks: -

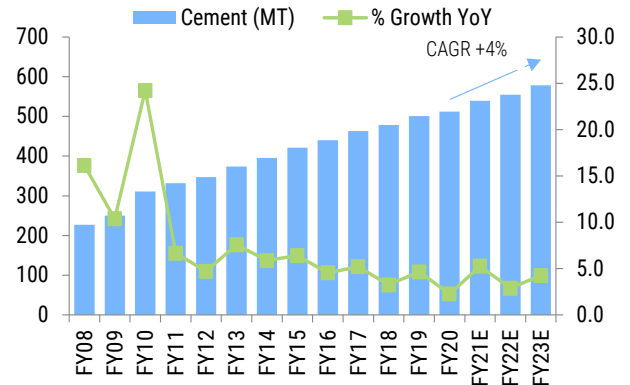
- Sudden spike in raw material prices can hurt margins.
- Weakness in demand growth emanating from slowdown in real estate sector and infra related activities.

Chart2: Cement demand trends



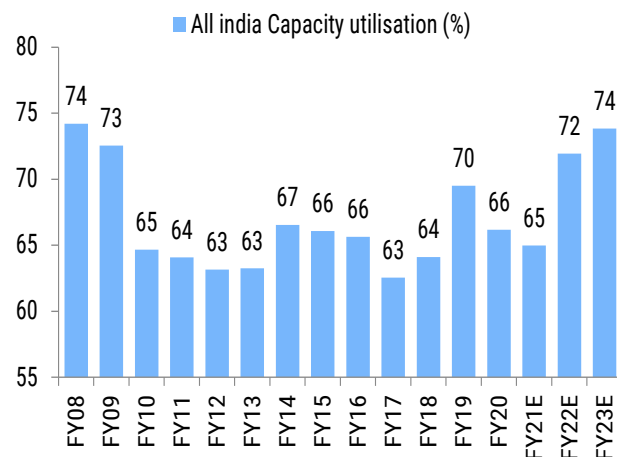
Source: JM Financial Research.

Chart3: Cement capacity trends



Source: JM Financial Research.

Chart4: Cement capacity utilization pan India



Source: JM Financial Research.

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