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Problems and Prospects of the Indian Cement Industry

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The cement industry is one of the core industries, which plays a vital role in the growth of a nation. In India too, cement industry plays a significant role in the overall growth of the economy. India is world's second largest cement producing country after China. The industry is characterized by a high degree of fragmentation that has created intense competitive pressures on price realizations. Spread across the length and breadth of the country there are 128 large plants belonging to 54 companies with an installed capacity of 184.2 million tones as on March 2008 and actual production of nearly 178.8 million tones for the year 2007-08.[1] Though India is the second largest producer of cement after China, per capita consumption of cement in the country is only 100 kgs As against the world average of 260 kgs. The per capita consumption of China is more than 450 kgs. Thus, there is a good potential for the cement industry in India itself. The principal reason for this optimism is the need for roads, bridges, highways and mass housing in a developing country like ours. Although the cement industry has recorded continuous growth since planning started yet the industry is facing many problems. In this research paper an effort has been made to identify the problems relating to the growth of cement industry and to know the prospects of the industry. It also includes the opportunities and threats for the industry in the present scenario.

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History of Cement Industry in India: Although the cement industry in India developed essentially after Independence, it owes its origin to British days. The first successful attempt to manufacture cement in India was made during 1913 when a factory was installed at Porbander (Gujarat). Before this, the entire demand for cement was met by imports from U.K., Belgium, Japan and Germany. However, shipping bottlenecks created by the war and the need for self-sufficiency necessitated the growth of the industry in India. The post war industrial boom gave a fillip to the industry resulting in the establishment of ten factories in India by 1924. But these units worked less than half of their rated capacity, perhaps due to people's low preference for indigenous cement. Thus, the bias for imported cement on the one hand and the competition among the producers on the other hand did a definite harm to the industry during the initial stage. The result was the closure of three factories. The industry asked for protection but could not get it. However, on the recommendations of Tariff Commission, Cement Manufacturers'

Association (C.M.A.) formed in 1925 and Cement Marketing Company of India formed in 1930 helped the industry through the regulation of price and distribution and other promotional efforts such as free technical aid and advice and educating the public in the uses of cement. An interesting turn in the cement industry came in 1936 when all the factories excepting one, sick of the cut-throat competition and in need of coordination, combined into a group, later known as the Associated Cement Companies Ltd. (ACC). We need hardly emphasize, that the formation of ACC resulted in lowering the cost of production, increasing uniformity in quality and infusing self-reliance.

Growth of the Cement Industry -: Although Production of cement in India commenced in the early part of the 20th century, but the industry registered significant growth only after the Five-year Plans were initiated, especially during the Sixth and Seventh Plans. Growth of cement industry during five-year plans is shown in Table-1& Graph-1

TABLE – 1

Growth of Cement Industry During Five year Plans

Year	Plan	Capacity at the End Of the Plan (Mn. Tone)	Production (Mn. Tone)	Production Growth (%)
1950-51	Pre Plan	3.28	2.20	N.A.
1955-56	Ist Plan	5.02	4.60	109.09
1960-61	II Plan	9.30	7.97	73.26
1965-66	III Plan	12.00	10.97	37.64
1973-74	IV Plan	19.76	14.66	33.63
1978-79	V Plan	22.58	19.42	32.47
1984-85	VI Plan	42.00	30.13	55.15
1989-90	VII Plan	60.55	45.25	50.18
1996-97	VIII Plan	105.26	76.22	68.44
2001-02	I X Plan	146.13	108.40	42.21
2006-07	X Plan	177.83	161.66	49.13

Source -: Cement Statistics –of CMA

Note -: There were Annual Plans for 1966-1967, 1967-1968, 1979-1980, 1990-1991 & 1991-1992.

GRAPH –1

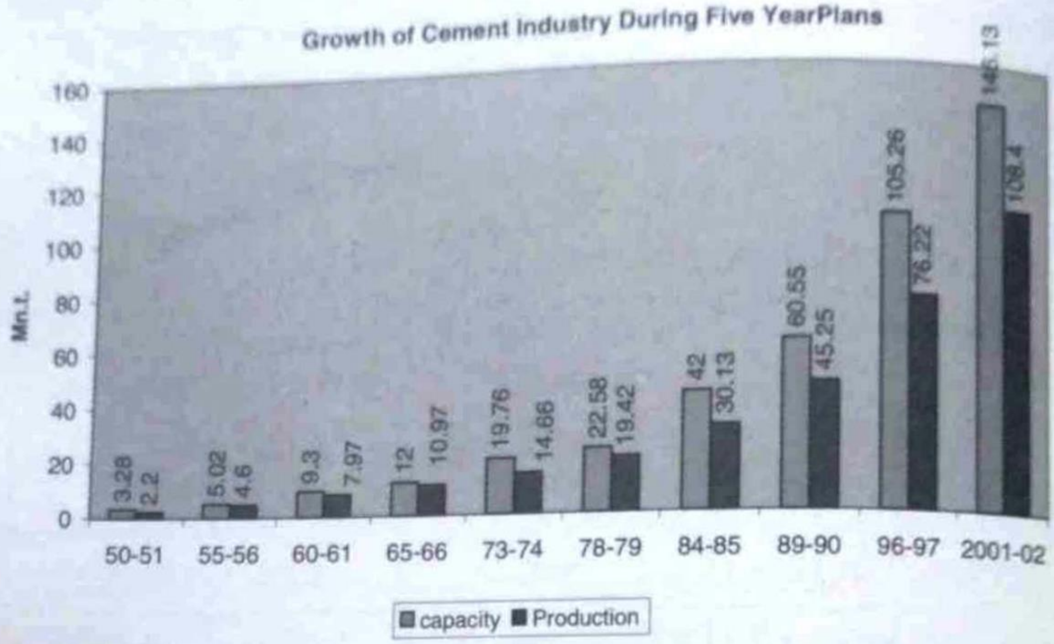


Table-1 & Graph-1 indicate initial installed capacity which was around 3.3 million tonnes at the beginning of the First Five year Plan has crossed 50 million tonnes during the Sixth and Seventh plans. Installed capacity has crossed 100 million tonnes during Eighth plan, crossed 135 million tonnes in the end of March 2002 and crossed 175 million tones by the end of the Tenth Plan (Year 2002-2007). [2]

Problems of Cement Industry: Though an important core industry of the nation, Indian cement has a fluctuating career, with years of prosperity alternating with years of depression. In the past, Indian cement industry has suffered from many problems. The important problems among them are Demand-supply imbalance, Cost escalation and rigid prices, Partial control and dual pricing and Unrealistic distribution policies of the government. I shall briefly discuss these problems and the attempts by the industry and the Government to solve them.

Demand-Supply imbalance: As we know, Indian Cement Industry has suffered from Demand-Supply imbalance. The problem of the cement industry has been that the supply of cement, ever since its inception has not been able to catch up with demand. The reason for this ever-widening gap between demand and supply cannot be entirely attributed to either of them. Neither are the estimates of demand quite precise at the time of fixing targets, nor is the supply commensurate with the capacity. Till the end of fifth plan (1974-78) demand of cement continued to remain in excess of supply. The slow growth in capacity and production during the mid 70's resulted in the shortage of cement (10% to 25% of annual consumption) and the country had to import about one to three million tonnes of cement per annum during 1978 to 1983.[3] The cement industry witnessed significant capacity addition during sixth and seventh plans (1984-85 to 1989-90). Capacity additions were also high in the period 1993-94 to 1996-97. Capacity added in 1995-96 and 1996-97 were particularly high at around 10 million tonnes and 8 million tonnes respectively. Due to high capacity additions in these years supply outstretched demand in the subsequent years. As a result prices began to slip as these capacities started adding to the production. However, capacity addition slowed down in 1997-98 due to delay in some projects and cancellation of several others following over capacity in the industry. New capacity additions in 1998-99 and 1999-2000 were on account of completion of the pending projects. However, the cement industry is slowly recovering as capacity additions have slowed down considerably and demand is catching up with supply. The consumption of cement grew at a compound annual growth rate (CAGR) of around 8% during the last decade. Whereas the cement demand growth in the last few years has been highly encouraging, the financial performance of the industry has been unsatisfactory primarily on account of mismatch between demand and supply. The details are given in Table -2

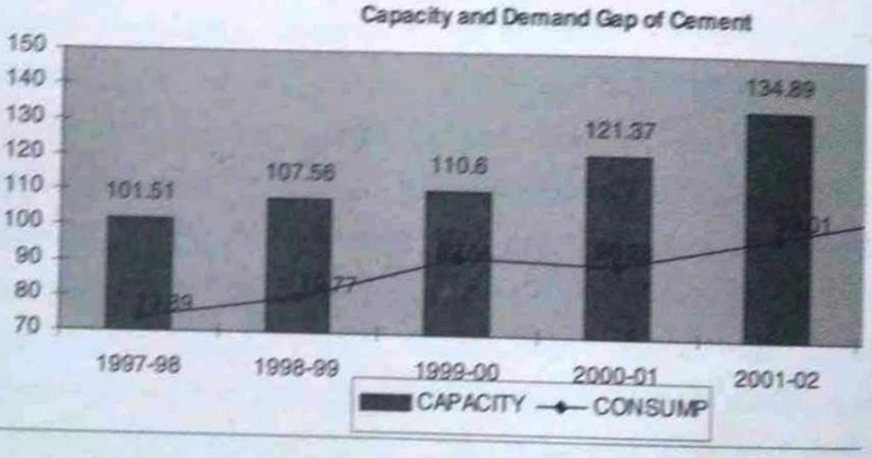
TABLE–2

Capacity And Demand Gap of Cement

Year	Capacity (M.T.)	Consumption Demand (M.T.)	Gap (M.T.)	Consumption Growth (%)
1997 - 1998	101.51	73.89	27.62	8.37 %
1998 - 1999	107.56	79.77	27.79	7.96 %
1999 - 2000	110.60	92.05	18.55	15.39 %
2000 - 2001	121.37	90.28	31.09	-1.92 %
2001 - 2002	134.89	99.01	35.88	9.67 %
2002 - 2003	140.07	107.59	32.48	8.67 %

Source -: 42nd Annual Report of CMA [2002-03]

GHAPH –2



Source-: Table – 2

Table & Graph 2 indicates increase in capacity by 6.05 M.t and consumption by 5.88 during the year 1998-99. This results demand gap increased marginally by o.17 M.t. during the year 1998-99. While during the period 1999-2000 demand gap decreased significantly by

9.24 M.t. Demand gap decreased due to increase in consumption of cement by more than 15% and low capacity additions. During the year 2000-01 due to negative rate of consumption growth and addition of capacity by more than 10 M.t. demand gap increased significantly by 12.54 M.t. Demand gap increased also in the year 2001-02 due to high addition of capacity by more than 13 M.t. In the year 2002-03 demand gap decreased by 3.4 M.t. (9.5%) due to increase in consumption growth by 8.67% and low capacity addition.

Cost escalation and rigid prices: The cement industry is a capital-intensive industry. A green-field cement plant of the 1-mpta capacities requires an investment of around Rs.330 crores. Being a highly capital intensive industry a fair return on capital is essential for the cement industry to remain healthy and grow in line with demand. Cement industry is a highly energy intensive industry with power and coal alone accounting for around 60% of the variable cost. Freight and transport cost also form another major component of the cement price in different locations. As in the case of all other industries, there was huge rise in the cost of production of cement during the last decade. The major cost such as (price and freight on coal, power and wages covered by wage awards) rises were due to government policies. While during the last decade cement prices have not risen in proportion to increase in cost of inputs. The low prices of cement and increased cost of inputs (power, coal, freight) prevailing over the last few years has taken a heavy tool on the financial health of the Indian cement industry. Thus, due to increase in cost of inputs on the one hand and decline / stagnate of cement prices on the other; most of the cement units are incurring losses since long. Thus resulting mini cement plants and other medium sized cement units are either closed or near to be closed. Bigger sized units are consolidating their business and improving profitability either by acquiring other plants or by cost cutting exercises.

Price control system: Another problem of the cement industry related to the system of price control. Price regulation was based on the assumption of 85% capacity utilization. Despite all-out efforts of industry, there was a declining trend in capacity utilization due to infrastructural bottlenecks of power, coal and rail movement. The capacity utilization which was 90 percent in 1978 came down rapidly to 67 percent in 1981. It rose to 79 percent since then.[4] The industry could not be blamed for this in as much as it was entirely due to factors controlled by the government agencies (Such as shortage of coal, load shedding and transport bottlenecks). The Government was the greatest beneficiary of price control of cement due to the single biggest consumer of cement in the country. Price control of cement resulted in unnecessary loss of the industry.

Unrealistic distribution policies: Another problem of the industry related to unrealistic regulation of distribution of cement. The Government introduced a permit system of distribution which never worked properly. After a lot of delay, the Government announced a scheme of partial decontrol with effect from February 1982 and introduced dual pricing in cement- levy cement for Government and small house builders and free open market cement for general consumers. According to this scheme levy quota was fixed at 66.6 percent of the cement produced by a factory in the case of existing units and 50 percent in the case of new and sick units and the balance percent of production could be sold in the open market. The levy quota was sold at controlled prices to the Government and other private sectors. The open sales were at higher market prices. The higher free sales prices were meant to cover up the rise in costs and help the cement units to generate additional internal resources; they would also help cement units to increase production to derive maximum benefit from open market sales. The scheme of partial control followed up with progressively reducing price and distribution controls on cement industry. This policy incentive resulted in significant progress both in terms of addition of new capacity and increased production. Since the country has reached self-sufficiency in cement, all price and distribution controls were withdrawn from March 1989. By decontrolling the cement industry, the government relaxed the forces of demand and supply. The industry responded positively to the encouragement given by the Government and consequently the last two decades witnessed a growth in cement production by nearly 70 million tones whereas during the previous three decades, cement production grew by less than 20 million tones.[5]

Inadequate Production: In recent years cement industry is facing the problem of inadequate production. The main factors responsible for shortfall in production are follows:

(I) Drastic power cuts ranging from 20 to 75 percent in various cement producing states.

(II) Shortage of coal.

(III) Inadequate availability of wagons.

(IV) Limited availability of furnace oil.

All these factors played their part in affecting bottom lines throughout the industry resulting in partial or complete closure of many units. However, the cement industry is slowly recovering as capacity additions have slowed down considerably and demand is catching up with supply. The top five players now control about 65-70% of the industry.[6] In the presently competitive global environment Indian cement industry has to face global competition and challenges. To meet out this challenge Indian cement industry should make its presence in more and more countries and for this; it has to be globally competitive. In this globalize scenario there are many opportunities as well as threats for the Indian cement industry. Following are the possible opportunities and threats for the cement sector.

Opportunities for Cement Sector:

Though India is the second largest producer of cement after China, its per capita consumption hovers around 102 Kgs. only as compared to about 450 Kgs. for China and world average of about 260 Kgs. Some of the developing countries are even having higher per capita consumption in excess of 500 Kgs. The low per capita consumption in India presents a fabulous opportunity for the sustained growth of the cement industry in future. The consumption of cement grew at a Compounded Annual Growth Rate (CAGR) of around 8% during the last decade. The growth of the cement industry over the years has shown close links with the overall economic performance of the country. Housing and infrastructure are the key growth drivers of cement industry. Rural housing demand is largely depend on good rainfall and consequent agricultural output. The planned infrastructure projects of road, airports, ports and power generation should push cement demand further. The continuation of fiscal benefits for promoting housing, lower housing finance rates, sustained growth in disbursements of housing finance etc will give a fillip to the cement demand growth. Looking to the various infrastructure projects, which are in the pipeline and the thrust being given to the road network and housing, high growth in cement consumption in the coming years is anticipated. The rising capacity utilization levels of leading cement players, with no new large capacities being created are expected to bring about Lester costs and more remunerative and stable cement prices in view of the narrowing down of the supply demand gap. Due to the expected rise in profits this will also made the units economically more viable.

There has been an opportunity of the industry in the international markets. Though Indian cement industry ranks 2nd in cement producing countries of the world, it accounts for only around 5.5% of the world exports. So there is a good potential for the export of cement and clinker. The industry's export performance during the year 2002-03 has been praiseworthy with the combined cement and clinker exports reaching the 7 million tonnes with growth of 34.63%.[7] The industry could have performed even much better but could not due to certain factors beyond industries control viz. high government levies, infrastructure bottlenecks rail/road/sea/port and administrative and procedural delays. For the first time, Indian cement could penetrate Taiwan and Turkey; themselves cement exporters, though in a small way. This is no less praiseworthy.

Threats / Risks for Cement Sector:

In the event of continued high prices for crude oil and other petroleum products, hardening of the coal prices and freights in the international markets, transport constraints in regard to movement of raw materials and products, and worsening fiscal position, the growth trajectory of the industry may be affected. Any delay/slowdown in implementation of the ongoing infrastructure development projects may result in raising the cost structure of cement production and reduced cement demand. Any bottlenecks in rail or road transportation will adversely affect the availability of coal and other inputs as well as the delivery of cement to consumption centers.

Owing to the general economic slowdown financial institutions tightened their credit norms. This led to a credit crunch and impacted upcoming real estate, infrastructure and other projects. With that, demand for cement moderated.

Cement continues to be one of the highest taxed commodities in our country with levies of around 25% to 30% of its price and any increase in these taxes/duties may adversely impact the profitability of the industry.

The fortunes of the cement industry are closely linked with the growth of the economy. In the highly unlikely event of the country going into deep recession, the cement demand may be adversely affected, which may also impact the cement prices.

Another major problem faced by the industry is the increase in cost of inputs. During the past few years the costs of raw materials, coal and power have been increasing at an alarming rate, which has led to a consistent decrease in the margin of profit for the cement industry. The burden of interest cost is also high on the industry. Any increase in these costs further adversely affects the operating margins of the industry.

The entrance of Multinationals with very huge plants is also a threat to the domestic suppliers as the MNC's will be able to reap the advantages of economies of large scale.

Conclusion: It can be concluded that although an important core industry of the nation, Indian cement has a fluctuating career, with years of prosperity alternating with years of depression. In the past, Indian cement industry has suffered from many problems such as Demand-supply imbalance, Cost escalation and rigid prices, Partial control and dual pricing and unrealistic distribution policies of the government. Besides, in recent years cement industry is facing the problem of inadequate production. The main factors responsible for shortfall in production are shortage of coal, inadequate availability of rail wagons, limited availability of furnace oil and drastic power cuts ranging from 20 to 75 percent in various cement producing states. Despite these problems the Indian cement industry is the 2nd largest market after China. It had a total capacity of about 260 Million tonnes (MT) in FY10. Despite the fact that the Indian cement industry has clocked production of more than 100 MT for the last five years, registering a growth of nearly 9% to 10%, the per capita consumption remains poor when compared with the world average and is almost 7 times lower than that of China. This underlines the tremendous scope for growth in the Indian cement industry in the long term. In recent years, the Government of India has given both direct and indirect encouragement to the cement industry. The indirect benefits have been in the form of demand push by given priority to infrastructure and housing sectors. Housing and infrastructure are the key growth drivers of cement industry. The planned infrastructure projects of road, airports, ports and power generation should push cement demand further. The continuation of fiscal benefits for promoting housing, lower housing finance rates, sustained growth in disbursements of housing finance etc will give a fillip to the cement demand growth. The demand for cement, therefore, is likely to grow faster than in the past. So it believes that Indian cement industry shall boom again in near future and the coming years will see the fashioning of a growth phenomenon. All in all, the future for cement looks very bright

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