

China Cement Weekly: Phasing Out of Lower Grade Cement on Track

Week ended 17 Jan. 2014

23 January 2014

Cement prices fell 0.3% in China last week and the 4WMA dipped 0.3% w/w. South Central and South Western China dipped 0.9% and 1.1% respectively while other regions remained stable. Inventory levels across China increased by 1.4 ppts to 65.4% as shipments slowed ahead of Chinese New Year.

Big players' supply discipline and lower inventories to support prices in low season. While overall inventory levels across China have gradually increased, price declines have been softer than last year. We believe this is down to lower inventory levels and improved execution of supply discipline among the big players. Most regions have announced schedules for 1Q14 production halts, which will last about as long as last year (*Figure 3 overleaf*). Cement prices will likely show some seasonal weakness in the next couple of weeks as construction work is put on hold for the New Year. But we expect less pressure on 1Q14 prices than in 1Q13 in view of: 1) higher prices than last year (up 11.6% y/y); 2) irregular production halts due to high pollution levels; 3) less new supply, 4) lower inventory levels than last year.

Draft released for new cement product standards; further progress on phasing out lower-grade cement. China Building Material Academy has released a draft of its new standards for cement products, which states that 32.5 grade cement (32.5 grade and 32.5R grade) will be cancelled. The new standards are expected to be approved by June 2014 and launched in 2H14. The draft came earlier than we expected, which underlines China's determination to curb sector overcapacity. 32.5 grade cement accounts for ~50% of cement production in China and consumes less cement clinker than 42.5 grade cement. We estimate that if 32.5 grade cement had accounted for only 25%, rather than 50%, of Chinese production in 2013, 8% more cement clinker would have been consumed. We expect the shift in product mix to further improve capacity utilization and ease cement overcapacity.

Our cement stock index rose 12.6% last week vs. the HSI's 1.3% gain. The sector trades at 8.4X forward P/E, below its average of 10.2X. China recently announced FAI numbers, with growth slowing from 20.6% in 2012 to 19.6% in 2013. This and possible liquidity tightening pose uncertainties about demand growth for cement. But we are more sanguine given a number of indicators that supply/demand dynamics are turning more favorable in 2014, including: 1) cement clinker capacity growing slower than demand; 2) improving capacity utilization driven by the phasing out of lower-grade cement and ongoing capacity shutdowns. Short-term sector catalysts include China's new urbanization plan, which is expected to be announced around Chinese New Year, and further policy detail after the NPC and CPPCC meetings in March. We continue to like **Anhui Conch (914.HK, Buy, TP: HK\$33.00)**, given its strong presence in Eastern and South Central China, which have the most favorable supply/demand dynamics. We also like **BBMG (2009.HK, Buy, PT: HK\$6.60)**. Cement prices in Hebei, one of its major markets, have lagged other regions but are likely to bottom out given: 1) likely further capacity shutdowns in the province in response to emission controls, after the current low season; 2) a raft of small, lower-grade cement operators in Northern China will be driven out of the industry in 2H14 once 32.5 grade cement is canceled.

Cement Stocks Index



Stock performances

Company	Ticker	Price	1m (%)	YTD (%)
Anhui Conch	914.HK	31.25	8.1	7.1
CR Cement	1313.HK	5.63	4.9	6.1
BBMG	2009.HK	6.43	0.5	(7.3)
CNBM	3323.HK	7.86	(6.2)	(7.7)
SINOMA	1893.HK	1.59	(4.8)	(6.0)
WCC	2233.HK	0.98	(13.2)	(13.9)
China Shanshui	691.HK	2.94	(9.4)	(12.9)
TCC	1136.HK	3.86	1.3	1.6
Asia Cement	743.HK	4.9	(0.4)	0.0
China Tianrui	1252.HK	2.28	11.2	(4.6)
Allied Cement	1312.HK	1.93	(13.1)	(8.3)

Sources: Bloomberg and Sun Hung Kai Financial

Recent Research

Company and Sector Reports

[2014 Sector Outlook – 17 Jan. 2014](#)

[Anhui Conch \(914.HK\): Sector Fundamentals Improving: Conch Our Top Pick – 31 Oct. 2013](#)

[BBMG \(2009.HK\): TP Reduced to HK6.60: Maintain Buy – 2 Sep. 2013](#)

[BBMG \(2009.HK\): 1H13 Results First Glance – 22 Aug. 2013](#)

[Anhui Conch \(914.HK\): 1H13 Post-Results Presentation – 21 Aug. 2013](#)

[Anhui Conch \(914.HK\): 1H13 Results In Line – 16 Aug. 2013](#)

[BBMG \(2009.HK\): Northern Exposure – 16 July 2013 \(Initiation of Coverage\)](#)

[Anhui Conch \(914.HK\): Opportunity to Accumulate – 4 June 2013](#)

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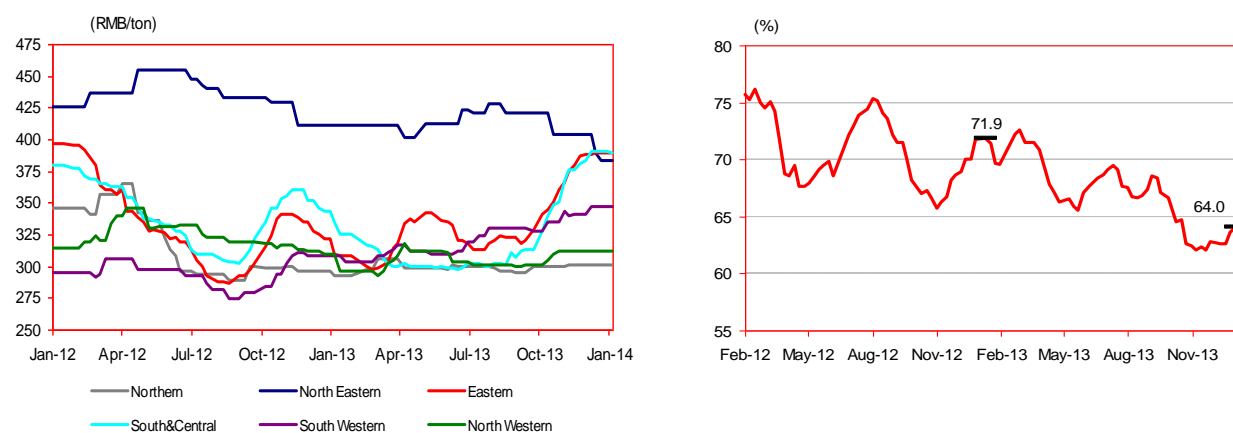
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Bloomberg Code: <shkr>

Figure 1: China cement price changes (week ended 17 Jan. 2013)

RMB/ton	China	Northern	North Eastern	Eastern	South Central	South Western	North Western
Current price	353.9	301.0	382.5	388.9	385.4	342.5	312.0
y/y	11.6%	3.1%	-6.9%	26.0%	18.4%	11.4%	5.6%
YTD	-0.6%	0.0%	-1.7%	0.0%	-1.4%	-1.1%	0.0%
w/w (4W mavg.)	-0.3%	0.0%	-1.3%	0.0%	-0.3%	-0.3%	0.0%
w/w	-0.33%	0.0%	0.0%	0.0%	-0.9%	-1.1%	0.0%

Sources: Digital Cement and Sun Hung Kai Financial

Figure 2: China – cement price trends (L) and inventory level (R)

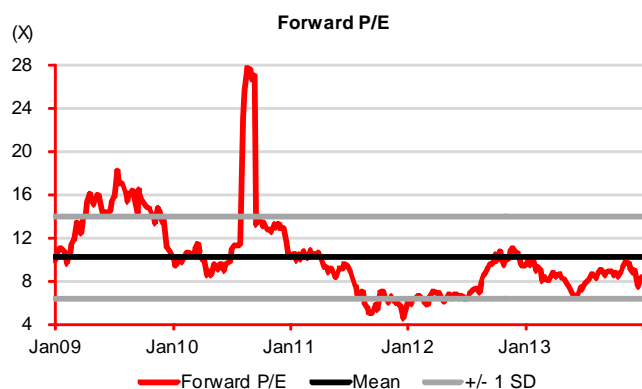
Sources: Digital Cement and Sun Hung Kai Financial

Figure 3: China – schedule for production halts by region

Region	Schedule for production halts
Northern China	
Hebei	No unified schedule for production halts in 1Q14. Big companies have halted production while they replenish clinker inventory. Production will also depend on the regional pollution levels.
Shanxi	Production in Taiyuan has been halted for one month to curb pollution levels.
North Eastern	
Liaoning	Four months in winter.
Eastern China	
Zhejiang	30 days from 25 January.
Jiangsu	35 days in 1Q14 as cement clinker inventory is replenished.
Jiangxi	30 days in 1Q14.
Anhui	30 days in 1Q14
Shandong	30 days for each production line, starting from 1 January.
South Central	
Henan	30-35 days in 1Q14.
South Western	
Sichuan	No fewer than 30 days in 1Q14.
Yunnan	20-40 days around Chinese New Year.
Guizhou	20-40 days around Chinese New Year.
North Western	Production mostly stopped due to the end of construction season.

Sources: Digital Cement and Sun Hung Kai Financial

Figure 4: Hong Kong-listed cement sector forward P/E (Next Annual)



Sources: Bloomberg and Sun Hung Kai Financial

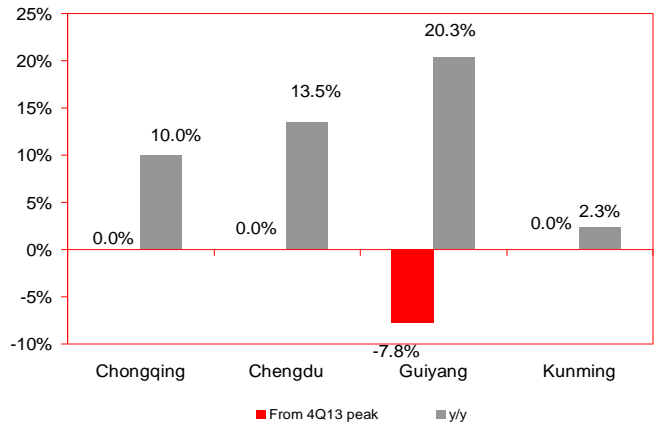
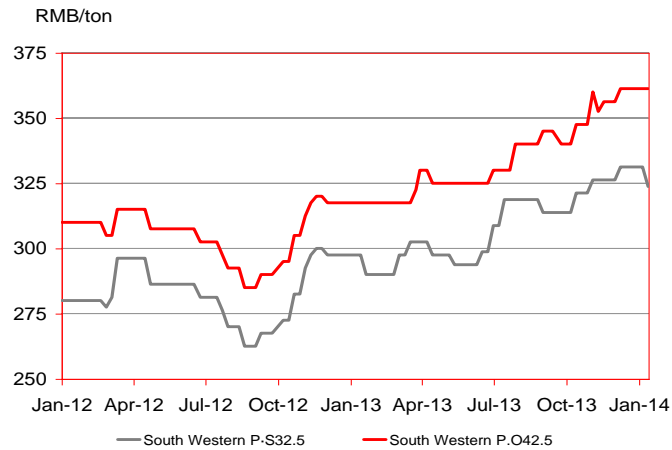
Figure 5: Peer valuations

		Price (LC)	Market cap (US\$m)	YTD (%)	FY1 EPS growth (%)	FY2 EPS growth (%)	FY1 P/E (X)	FY2 P/E (X)	FY2 EV/ EBITDA (X)	Div yield (%)	P/B (X)	ND/E (%)	ROE (%)
Hong Kong-listed													
Anhui Conch-H	914.HK	31.25	16,204.6	8.7	41.9	19.5	14.4	12.1	6.0	1.0	2.6	30.7	13.6
CR Cement	1313.HK	5.63	4,741.5	8.1	33.9	17.2	11.8	10.1	7.3	1.9	1.6	84.9	11.4
BBMG-H	2009.HK	6.43	4,025.6	(4.7)	(6.4)	19.5	7.8	6.5	7.0	1.6	0.9	79.7	13.8
CNBM-H	3323.HK	7.86	5,470.6	(5.8)	(0.8)	18.1	6.0	5.1	8.3	2.5	1.1	326.4	19.6
SINOMA-H	1893.HK	1.59	732.1	(4.8)	(1.5)	26.0	9.5	7.5	5.7	2.4	0.4	89.0	4.3
West China	2233.HK	0.98	574.5	(14.8)	18.1	24.5	7.8	6.3	5.1	2.6	0.7	72.2	8.3
China Shanshui	691.HK	2.94	1,067.3	(11.7)	(34.8)	15.6	6.5	5.6	5.0	8.1	0.7	132.3	18.6
TCC	1136.HK	3.86	1,639.9	1.6	118.3	14.7	9.9	8.7	6.5	1.6	0.8	68.1	3.9
Asia Cement	743.HK	4.90	983.1	0.2	101.6	31.0	7.6	5.8	4.9	2.6	0.7	49.2	4.6
Tianrui Cement	1252.HK	2.28	705.7	(5.0)	(18.2)	22.2	6.6	5.4	6.4	0.0	0.6	142.4	13.2
Allied Cement	1312.HK	1.93	164.2	(10.6)	N/A	N/A	N/A	N/A	N/A	1.0	1.7	(44.4)	4.1
Average				(3.5)	25.2	20.8	8.8	7.3	6.2	2.3	1.1	93.7	10.5
A-share market													
Anhui Conch-A	600585.CH	16.60	16,204.6	(2.1)	42.9	22.5	9.8	8.0	6.2	1.5	1.8	30.7	13.6
BBMG-A	601992.CH	5.94	4,025.6	(12.6)	1.7	13.2	8.5	7.5	9.3	1.2	1.1	79.7	13.8
Tangshan Jidong	000401.CH	7.54	1,678.6	(11.1)	57.5	101.9	35.7	17.7	8.5	1.3	0.9	152.7	1.6
Huaxin	600801.CH	11.11	1,597.5	(8.5)	74.1	22.5	10.8	8.8	5.2	1.6	1.3	91.1	7.2
Jilin Yatai	600881.CH	3.88	1,214.6	(1.0)	N/A	N/A	N/A	9.9	N/A	2.6	0.9	182.6	5.3
Gansu Qilianshan	600720.CH	6.70	859.3	0.1	137.1	17.0	12.6	10.8	6.4	0.7	1.3	92.5	5.3
Wannianqing	000789.CH	9.44	637.7	(0.2)	101.5	28.6	9.8	7.6	4.8	1.1	2.0	72.6	11.2
Average				(5.1)	69.1	34.3	14.5	10.0	6.7	1.4	1.3	100.3	8.3

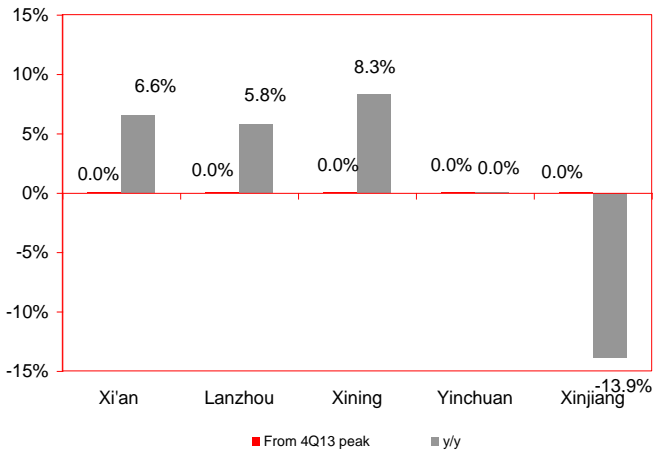
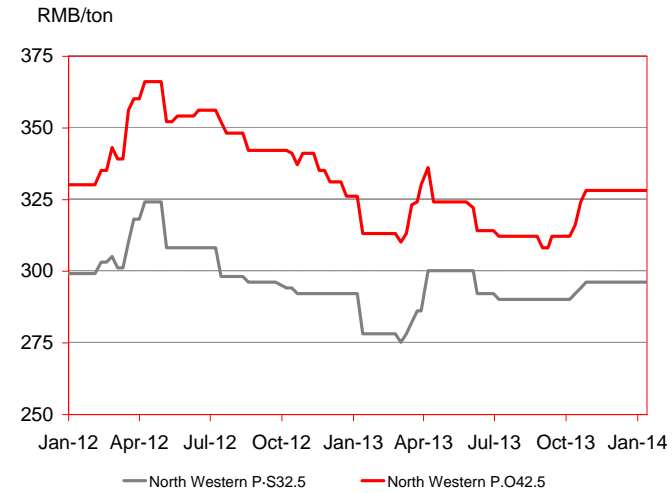
Sources: Bloomberg and Sun Hung Kai Financial

Figure 6: China – cement prices by region

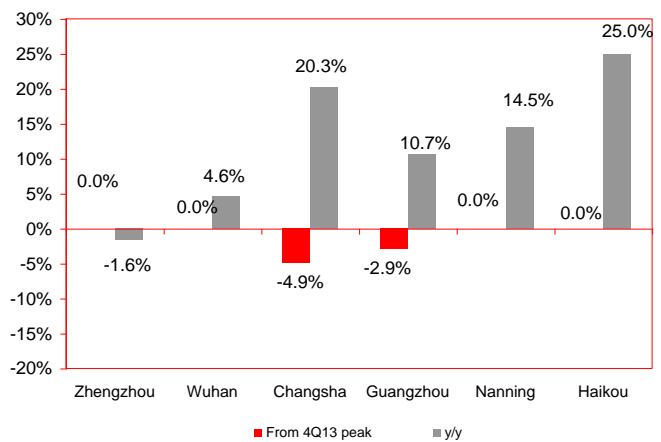
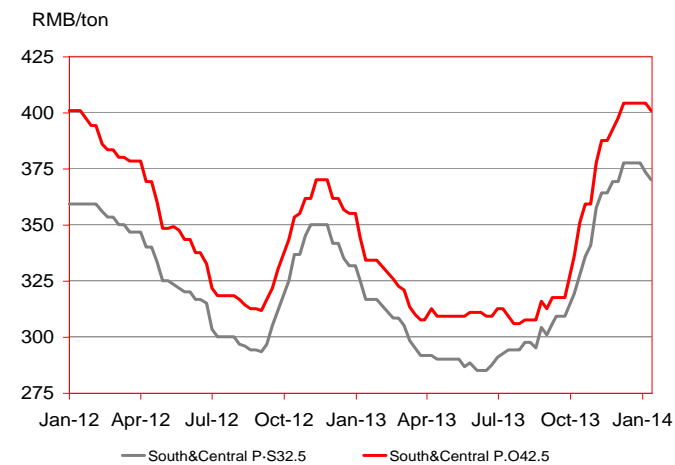
Southwestern China



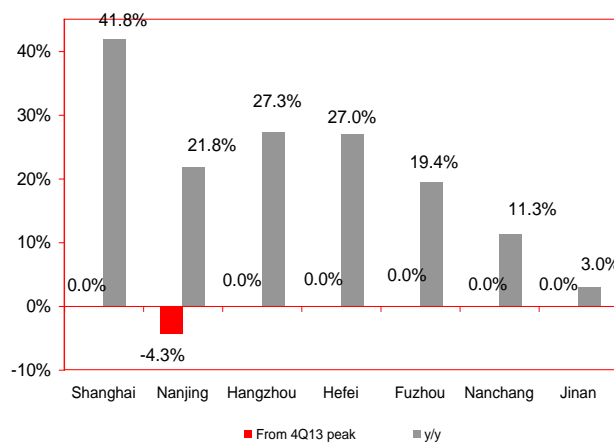
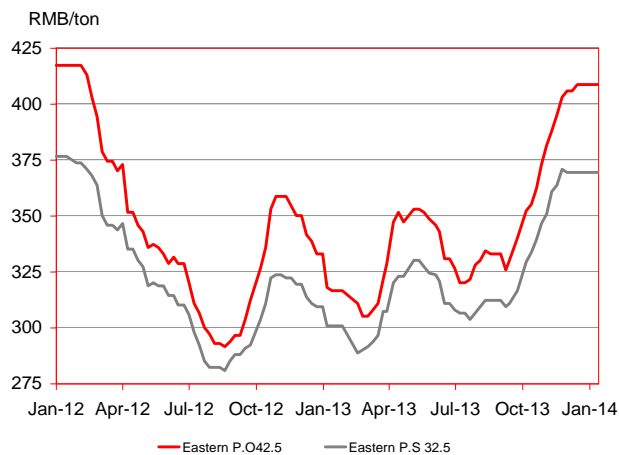
Northwestern China



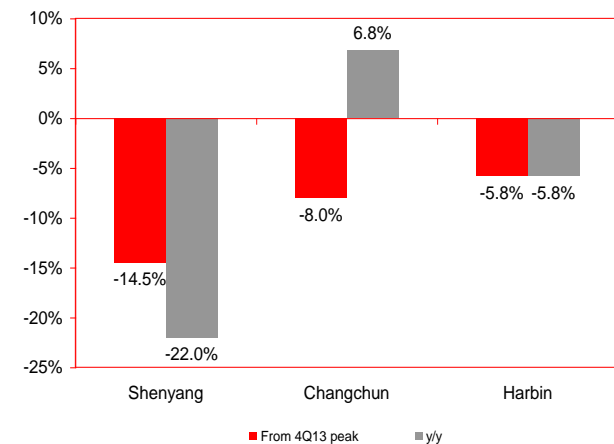
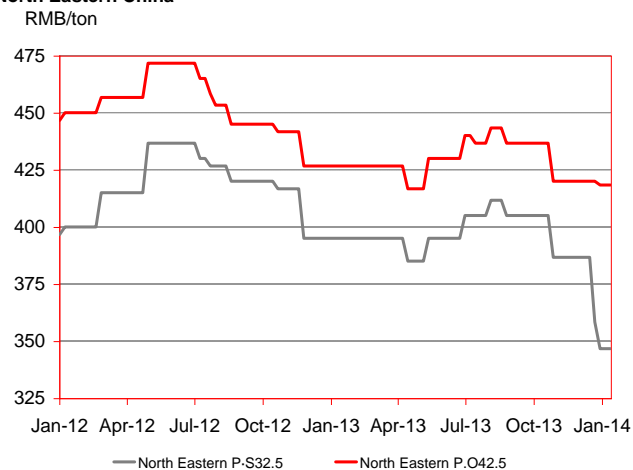
South & Central China



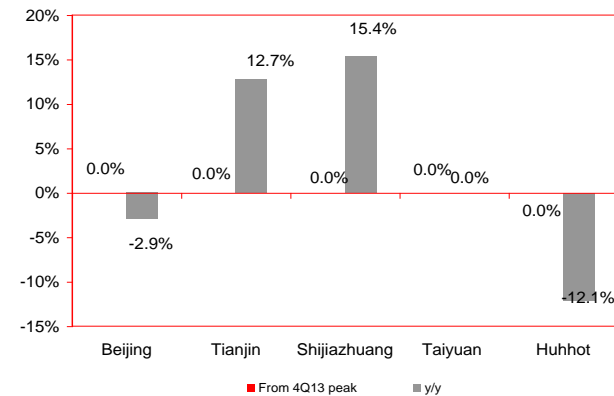
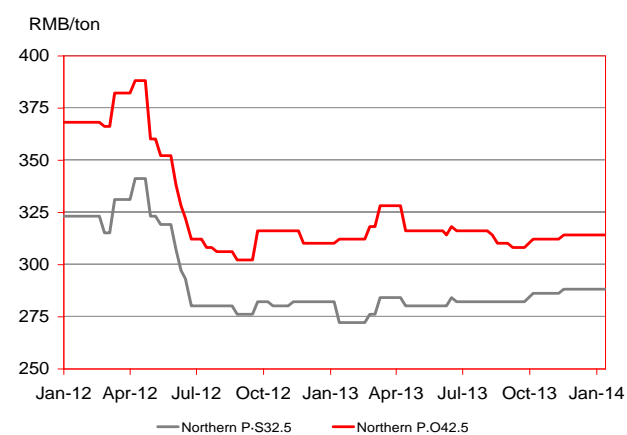
Eastern China



North Eastern China



Northern China

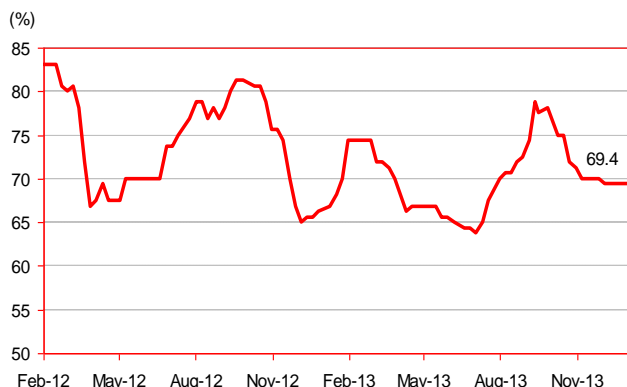


Sources: Digital Cement and Sun Hung Kai Financial

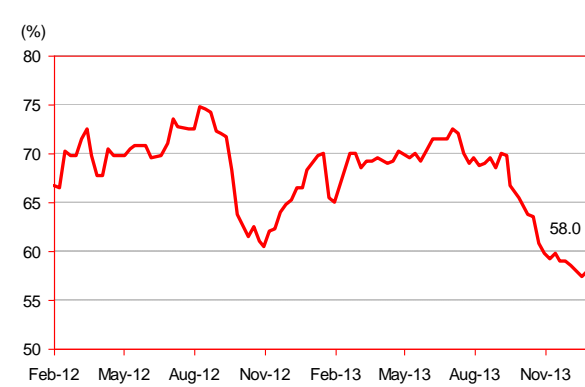


Figure 7: China – Cement inventory level by region (inventory-to-warehouse-capacity ratio)

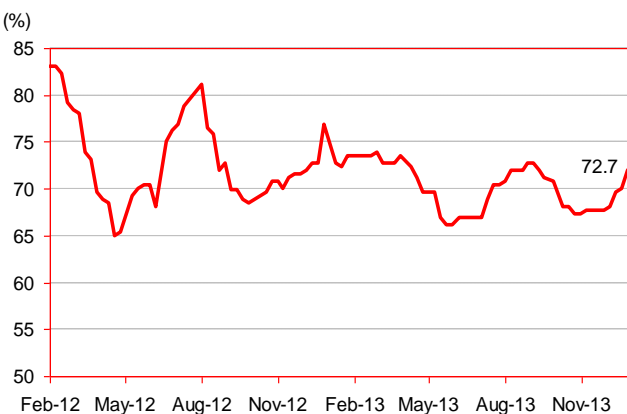
South Western China



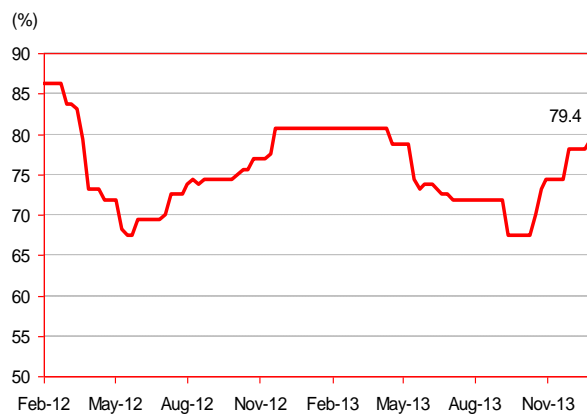
South Central China



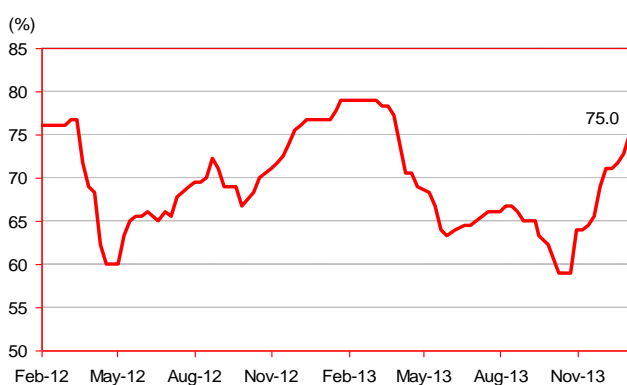
Northern China



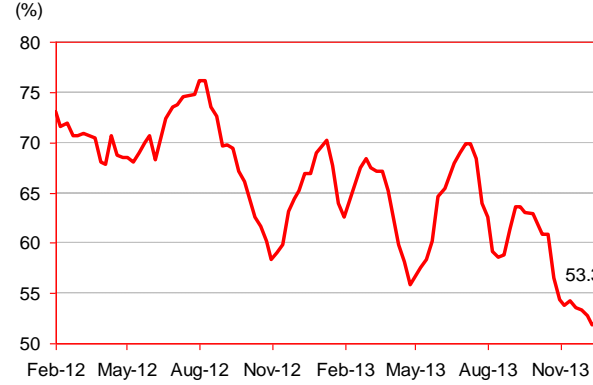
North Eastern China



North Western China



Eastern China



Sources: Digital Cement and Sun Hung Kai Financial



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