ATIF MUNIR, CEMENT PAKISTAN COMPANY,

OUTLINES THE CURRENT STATUS OF PAKISTAN'S CEMENT INDUSTRY, ITS CHALLENGES AND EXPECTATIONS.

A COMPREHENSIVE REPORT ON PAKISTAN'S CEMENT INDUSTRY

Cement is one of the most advanced and well established industries of Pakistan. Besides playing a key role in the development of physical infrastructure and generating economic activity in a number of downstream industries (especially construction), it also contributes significantly towards generating revenue for the government. The cement industry has integrated production facilities based on locally available raw materials. Pakistan's cement industry has undergone continuous technological transformation and upgradation and has acquired modern dry process technology from European suppliers.

History

The cement industry in Pakistan has grown gradually over time. At the time of independence in 1947, there were only four cement plants with a total production capacity of nearly 0.5 million tpa. By 1972 the number of cement plants increased to 14 and the production capacity also increased to 2.5 million t but could not keep pace with the country's economic development. Both public and private sectors took the initiative to establish new plants. As was the case for other industries, the cement industry was nationalised in 1972 and the "State Cement Corporation of Pakistan" (SCCP) was established and given the responsibility for the production of cement in the country. Considering the higher cement demand as compared to supply, cement import was also allowed in FY76 - 77 and continued until FY94 - 95. With a change in policy of state control over industrial units, the state-owned cement plants were put up for privatisation along with other industries. The private sector was allowed to invest in cement manufacturing. Consequently, the role of SCCP as market leader vanished gradually and currently it owns only four plants, of which two have been closed down on efficiency and profitability grounds. In view of the higher demand during the period of deregulation and liberalisation, a number of new

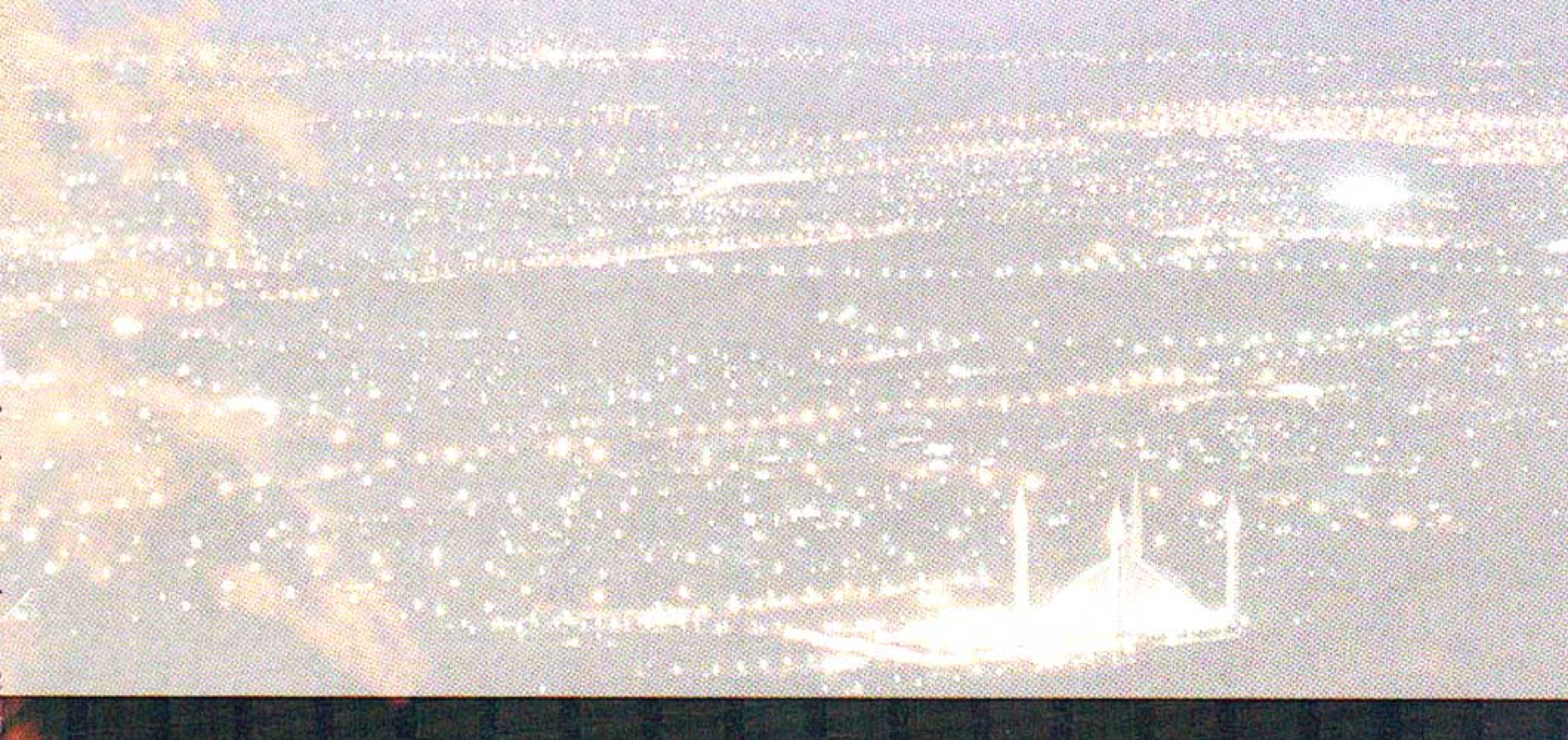


Table 1. Installed production capacity of cement plants in Pakistan			
North zone			
Sr. no.	**Name of unit**	**Production capacity to July 2009**	
		Clinker (million t)	**Cement (million t)**
1	Askari Cement Limited - Wah	1.050	1.1025
2	Askari Cement - Nizampur	1.5	1.575
3	Bestway Cement Limited - Hattar	1.17	1.2285
4	Bestway Cement Limited - Chakwal	3.4284	3.59982
5	Cherat Cement Company Limited-Nowshera	1.0	1.05
6	Dandot Cement Limited - Jehlum	0.48	0.504
7	Dewan Hattar Cement Limited - Hattar	1.08	1.134
8	D.G.Khan Cement Limited - D.G.Khan	2.01	2.1105
9	D.G.Khan Cement Limited - Chakwal	2.01	2.1105
10	Fauji Cement Company Limited - Fateh Jang	1.11	1.1655
11	Fecto Cement Limited - Sangjani	0.78	0.819
12	Flying Cement Limited - Lilla	1.2	1.26
13	GharibWal Cement Limited - Jehlum	2.55	2.6775
14	Kohat Cement Company Limited - Kohat	2.55	2.6775
15	Lucky Cement Limited - Pezu	3.725714	3.912
16	Maple Leaf Cement Factory Limited - Daudkhel	3.51	3.6855
17	Mustehkum Cement Limited - Hattar	0.465	0.48825
18	Lafarge Pakistan Cement Company Limited - Chakwal	1.95	2.0475
19	Pioneer Cement Limited - Khushab	1.933571	2.03025
Sub total (North)		**33.502686**	**35.17782**
South zone			
1	A.C. Rohri Cement Limited - Rohri	0.23	0.2415
2	Al-Abbas Cement Limited - Nooriabad, Dadu	0.45	0.4725
3	Attock Cement Pakistan Limited - Hub Chowki, Lasbela	1.71	1.7955
4	Dadabhoy Cement Industries Limited - Nooriabad, Dadu	0.504762	0.53
5	Dewan Cement Limited - Dhabeji	0.75	0.7875
6	Javedan Cement Limited	0.6	0.63
7	Lucky Cement Limited, - Indus Highway, Karachi	3.428571	3.6
8	Pakistan Slag Cement Limited	-	0.1575
9	Thatta Cement Limited - Thatta	0.3	0.315
10	Zeal Pak Cement Limited - Hyderabad	0.342857	0.36
Sub total (South)		**8.31619**	**8.8895**
Grand total (North+South)		**41.818876**	**44.06732**

units were set up and many others invested heavily to increase their existing production capacity. After 2002 - 03, most of the cement manufacturers expanded their operations, and increased production. This sector has invested about US$1.5 billion in capacity expansion over the last six years.

The cement industry in Pakistan is divided into two broad regions, the Northern and Southern regions. There are 29 cement production units registered in the country with an installed production capacity of 44.07 million t. Of these, 19 units are located in the north with an installed production capacity of 35.18 million t (80%) while 10 units are located in the south with an installed production capacity of 8.89 million t (20%). There are four foreign companies, three armed forces companies and 16 private companies listed in the stock exchanges.

Due to political instability and lack of allocation of funds for the Public Sector Development Program (PSDP), the cement industry, which was in the recession phase, registered an average growth rate of 2.96% for the 1990 to 2002 period. The period from 2003 to 2009 has been a golden age for the Pakistan cement industry. During this period the industry has shown tremendous growth. The boost in the cement sector was initially due to rising construction activity in the country, reconstruction activity in neighbouring Afghanistan and, later, tremendous increase in exports of cement from Pakistan.

Total cement production in Pakistan has increased dramatically since 2001. During FY08/09, the total cement production was 41.76 million t, which is 12.4% higher than in the previous year. Total cement dispatches, including local sales and exports, showed a 47.02% increase in FY08/09 as compared to the previous year. However, it is interesting to note that during the same period, local dispatches decreased by 14.07%.

Currently, of the total production capacity of approximately 44 million t, domestic demand accounts for 19.39 million t, while the industry has exported about 11.38 million t over the last year. By 2010, after expansion and installation of new plants, the total annual cement capacity is expected to be around 51 million t.

Local sales

The main factors behind local cement dispatches are Public Sector Development Projects (PSDP) allocation, GDP growth, real estate development projects for commercial and residential use, and the anticipated construction of mega dams. Total local sales of cement in FY06/07 and FY 07/08 were 21 million and 22.5 million t respectively, which declined to 19.4 million t during FY08/09.

The 14.07% decrease in domestic cement consumption during FY08/09 can be attributed to the fact that big private projects are not currently under implementation and neither is the government fully utilising its budgetary allocation for the Public Sector Development Program (PSDP). Economic recession, political instability and the downfall of the real estate industry also contributed towards this negative growth.

According to experts, local cement dispatches are likely to improve in 2009 - 2010 due to an increase in Public Sector Development Program allocation (Rs.621 billion) in the budget FY09/10 and a reduction in excise duty by Rs.10 per bag, as well as declining interest rates. Local demand for cement is also expected to be on the high side due to the reconstruction activities of devastated homes and buildings in the Northern region after the recent military operation. The growth in cement dispatches is solely attributable to rising export volumes, as domestic demand remained depressed in every comparable time period. Overall, cement plants of Pakistan operated at 73.69%

Table 2. Historical data from 2000 – 2009: Pakistan's cement industry

July to June	Production capacity (million t)	% increase	Local despatches (million t)	% incr/(dec)	Exports (million t)	% incr/ (dec)	Total despatches (million t)	% increase (total)	Capacity utilisation (%)	Surplus capacity (million t)
2000 – 2001	15.534	-5.16%	9.933	-0.04%	-	0.00%	9.933	-0.04%	63.95%	5.600
2001 – 2002	15.723	1.22%	9.833	-1.01%	0.107	100.00%	9.940	0.06%	63.22%	5.783
2002 – 2003	16.321	3.81%	10.980	11.66%	0.430	303.60%	11.410	14.80%	69.91%	4.911
2003 – 2004	16.936	3.77%	12.545	14.25%	1.160	169.52%	13.705	20.11%	80.92%	3.231
2004 – 2005	17.909	5.75%	14.788	17.88%	1.565	34.95%	16.353	19.33%	91.32%	1.555
2005 – 2006	20.955	17.01%	16.907	14.33%	1.505	-3.83%	18.412	12.59%	87.87%	2.543
2006 – 2007	30.251	44.36%	21.034	24.41%	3.188	111.83%	24.223	31.56%	80.07%	6.028
2007 – 2008	37.157	22.83%	22.596	7.30%	7.717	142.02%	30.286	25.03%	81.51%	6.871
2008 – 2009	41.760	12.39%	19.394	-14.07%	11.381	47.48%	30.775	1.61%	73.69%	10.986

capacity utilisation in 2008 – 09 as compared to 81.51% utilisation in 2007 – 08.

As cement capacity is increasing to cater to rising domestic and regional demand, the industry has started facing a tougher time, with a fall in prices after the second quarter of this fiscal due to increased supplies, surging energy prices and higher expansion, which led to mounting finance and depreciation costs. After reaching Rs.430 per bag at the retail level in 2006, cement prices fell sharply over the next few years to reach Rs.225 per bag in local markets.

Export sales

Unlike local sales, cement exports continue to make significant progress in 2009 despite the global economic recession. According to statistics from the All Pakistan Cement Manufacturers Association (APCMA), cement exports in 2008 – 09 increased to 11.38 million t, netting US$700 million, compared to 7.716 million t in 2007 - 08. Pakistan attained fifth position in the world's cement exports after a huge increase of 47% in exports during the last fiscal year. According to the *Global Cement Report*, China maintained first position with 26 million t in exports, while Japan got second position by exporting 12.6 million t of cement. The third largest cement exporter in the world is Thailand, with around 12 million t, followed by Turkey, which exported 11.6 million t of cement. Pakistan, now at fifth position, has left Germany behind by exporting more than 11 million t of cement during the last fiscal year. Germany now stands at sixth position with 9 million t exports.

Cement market experts have said that Pakistan secured this position because of high demand of cement in nearby countries and by capturing new markets such as African countries, Qatar and Iraq. Pakistan could achieve 13 to 14 million t exports by the end of the fiscal year, keeping in view the Indian market, which has once again started importing cement from Pakistan. (The export of cement from Pakistan to India showed a sharp decline after the Mumbai attacks.)

The weight of sea-based cement exports from Pakistan during July 2009 was recorded at 68% of overall cement exports, as compared with 63% in July 2008. It is important to note that cement exports to India during June 2009 were recorded at 70 085 t, which is low when compared with 97 413 t in June 2008.

Data for FY08/09 shows that Afghanistan is Pakistan's largest cement export market. Cement exports to Afghanistan increased by 15.27% and reached 3.201 million t as compared with 2.777 million t in 2007 - 08. Pakistan is the prime supplier for Afghanistan's cement requirement due to low cement production capacity and lack of a sea port in Afghanistan and feasible transportation charges of cement from Pakistan.

India is also a big potential market for Pakistan cement and constitutes 8.5% of Pakistan's total cement exports. Many cement manufacturers in Pakistan have already gained their product approval by BUREAU OF INDIAN STANDARDS, a requirement for exporting cement to India.

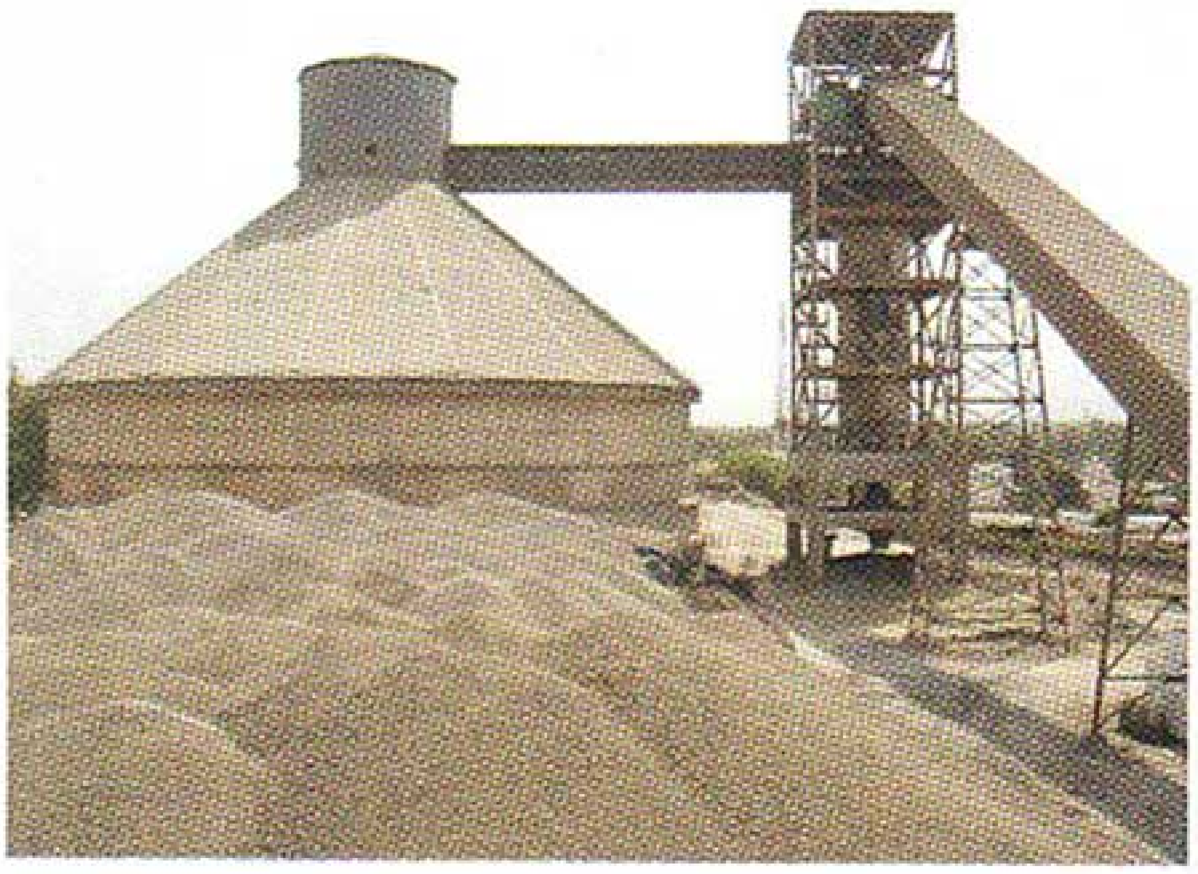
Pakistan achieved improved access to India after the complete removal of the 12.5% duty on Portland cement imports in January 2007. Unfortunately, the Mumbai attacks in November 2008 weakened the trade relation between Islamabad and New Delhi, and the re-imposition of 12% countervailing duty (CVD) by Indian Government on import of cement to support its indigenous industry also affected imports from Pakistan. However, in recent months the cement export activities from Pakistan to India have again started to increase due to market forces, which stabilise prices in the Indian market and keep a balance in demand and supply of cement.

Currently cement is being exported to India by land through the Wagah Border, while popular Indian ports for sea transportation are Nhava Sheva, Tuticorin, Cochin and Chennai. The major challenges to cement exports to India are the diplomatic relations between both countries, the 12% duty imposed by the Indian Government on cement imports, and the lack of proper infrastructure for cement transportation. All the cement being transported by land is first off-loaded by Pakistani trucks and then reloaded on Indian trucks on the other side of the border, which considerably increases costs. According to a trade understanding, for land transportation, both the countries are to provide train facilities on the basis of inter-change, which means that one engine would go from Pakistan and the other would come from India to carry cement and other commodities across the Wagah border. However, a shortage of rail-wagons on either side has put barriers on cement exports.

That being said, Pakistan is a favourite market for Indian cement importers. Keeping in mind the short delivery period and low freight charges to nearby Indian ports, the import of cement from Pakistan is likely to increase in the coming months.

Cement exporters are also eyeing the markets of Africa, the Middle East and Central Asia to enhance cement exports. The future growth of Pakistan's cement industry lies in the African markets. Africa's cement demand exceeds supply by as much as 7 million tpa. The construction industry there is growing at an average annual rate of 25%. The demand for Pakistan cement exports will be very strong in the wake of

Table 3. Local cement sales during July 2008 – June 2009	
Month	Total (t)
July 2008	1 791 200
August 2008	1 545 642
September 2008	1 497 468
October 2008	1 503 394
November 2008	1 603 945
December 2008	1 315 270
January 2009	1 596 539
February 2009	1 580 665
March 2009	1 810 245
April 2009	1 665 098
May 2009	1 648 088
June 2009	1 836 471
Total	**19 394 025**



Askari Cement, owned by the Army Welfare Trust, has a production capacity of 3000 tpd.

planned massive-scale construction; for example, the UAE will require around 26.2 million t by 2011. Similarly, South Africa requires a large amount of cement for the coming football World Cup event.

The government of Pakistan has already exempted cement exports from general sales tax (GST) and federal excise duty (FED) and now is expected to grant an inland freight subsidy in a bid to enhance cement exports. Pakistan's cement industry is set to achieve the US$1 billion cement export level due to the growth in demand on the international market. Cement exporters are expected to get inland freight subsidy from Rs.40 billion export investment fund announced in 2009 - 10 budget. Since the majority of cement production capacity is in the north zone, the factories pay high inland freight costs for exporting cement by sea; therefore, the industry needs support in the shape of freight subsidies in order to encourage exports.

The cement manufacturers have added 8 million t of new capacity and total production is expected to be 45 million t by the end of this year. Despite an excess supply of 11 million t in 2008, it is estimated that prices will increase in domestic as well as in regional markets, which would surely boost profitability and provide relief to the industry on its new investment.

Lucky Cement Limited

Whenever one discusses cement exports from Pakistan, it is necessary to highlight the role of Lucky Cement Limited, which maintains first position among cement exporters. The Lucky Cement Limited by (YB) Yunus Brothers Group started operating in 1996 with a production capacity of 1.2 million tpa at its mother plant in Pezu NWFP, which was subsequently upgraded to 1.5 million tpa in 1999. Lucky Cement Limited emerged as the largest manufacturer of cement in Pakistan in 2004 - 05 when the company underwent a massive expansion plan of 5 million tpa in one go, both at the Pezu plant with 2.5 million tpa and a new greenfield project of 2.5 million tpa in Karachi. The project in Karachi, near the port, was set up with the idea of exporting cement to the regional countries by sea. Immediately after getting a good response from the export markets, the company added another line of 1.25 million tpa at the Karachi plant to take the company's total capacity to 7.75 million tpa. The company, which accounts for a third of Pakistan's overseas cement sales, exported 57% of its production to the Middle East, Africa, Sri Lanka, India and Afghanistan in the nine months ending 31 March 2009. Sales to India, Sri Lanka and Egypt will continue to grow, as demand from the Middle East slows. The company also plans to acquire some local rivals to expand capacity at home.

Lucky Cement has given a new dimension to the local cement industry by exporting its product despite several bottlenecks. The bold decisions by management, taken at the right time, have maintained the company's competitiveness. It decided to set up its own export-related infrastructure on a self-finance basis, and purchased 75 bulkers and a ship loader, through which it started loose cement export for the first time in the country's history in February 2007. The encouraging performance of loose cement exports further motivated the management to invest in a storage facility at the port as buffer stock, together with the fastest loading machinery for quick turn-around to avoid waiting and loading time for sea going vessels. The Lucky Cement brand holds maximum certifications among Pakistani cement exporters and has been exported to over 22 countries around the world.

Lucky Cement now plans to strengthen its presence beyond the country's boundaries: Pakistan's biggest producer plans to start its first overseas factory in Africa by 2011. Muhammad Ali Tabba, the Chief Executive Officer of Lucky Cement said in an interview that Lucky, which exports to South Africa, aims to use the African factory to export to Europe. Africa, with a combined gross domestic product of US$2.68 trillion and a population of 987 million, is forecast to expand 4.5% next year, compared with 2.8% in 2009.

Challenges

Future challenges faced by the industry are coal and electricity charges and freight charges, which also comprise a large portion of the delivered cost. Major capacities of countries like Saudi Arabia and Iran are expected to come online by FY10 and onwards, which are likely to convert these countries from dependent importers to potential exporters.

Moreover, higher interest rates and inflationary concerns make it disadvantageous for investors to enter the construction industry. In addition to this, the decline of the real estate industry in recent years also poses a threat to the cement industry. The local real estate industry is also facing a tough time; the construction market has witnessed almost a 50% decline.

The industry should explore new markets for export or be ready to lower prices in the local market. The sharp decline in cement prices due to domestic competition among producers

Table 4. Export of clinker and cement from Pakistan during 2001 – 2009 (qty/tons)

Years	Cement			Clinker	Total	% Increase/ (decrease)
	Afghanistan via land	India via sea and land	Other countries via sea	Other countries via sea		
2001-2002	106 620	-	-	-	106 620	100.00%
2002-2003	430 332	-	-	41 500	471 882	342.53%
2003-2004	1 118 293	-	-	-	1 118 293	137.02%
2004-2005	1 407 900	-	157 270	-	1 565 170	39.96%
2005-2006	1 413 994	-	91 165	-	1 505 159	-3.83%
2006-2007	1 725 526	-	1 071 928	390 973	3 188 427	111.83%
2007-2008	2 777 826	786 672	3 045 995	1 106 127	7 716 620	142.02%
2008-2009	3 201 953	669 700	6 567 042	942 137	11 380 830	47.48%

has dampened the profitability of the industry. To cope with this situation, some manufacturers formed a cartel to set minimum cement prices. This translated into a marketing arrangement that increased cement prices despite lower or same operational costs. To break-up the cartel, in August 2009, the Competition Commission of Pakistan (CCP) imposed a penalty on 20 cement manufacturers for inflating cement prices as part of an agreement between manufacturing units. Each company has been asked to pay penalties equivalent to 7.5% of their last annual turnover, which amounts to Rs.6.3 billion.

Future

The capital structure of cement companies may change, as most of the expansions during the last two to three years have been debt financed and companies are expected to retire these debts rapidly over the next three to five years. Moreover, a slowdown in the economy may occur due to the global economic recession and political uncertainty in Pakistan, which might keep local sales low. However, if the hydro-powered dams are constructed, there will be a sudden jump in the local sales of those companies located near these dams.

The capacity utilisation has also improved to around an average of 80%. The Middle East, India and African countries have been the main market for Pakistani cement export.

The cement industry's installed capacity more than doubled during the last five years, which helped the industry achieve high export growth. Competitive rates of Pakistani cement have also helped in capturing the regional market. The government's decision regarding the restoration of the duty drawback has also raised the cement export and the reconstruction work in Afghanistan, and exploration of new African markets has led to an increase in cement exports. The Pakistani cement sector has been taking full advantage of these opportunities.

During the last two years, Iran and Saudi Arabia have implemented cement capacity expansion projects and are reckoned as a main source of cement supply to the Middle East in the future. The local cement industry therefore needs to take corrective measures for its sustainable development, on an emergency basis. The Government is also promoting export of cement. In continuation of these efforts, the Port Qasim Authority (PQA) and Pakistan International Container Terminal (PICT) are all set to sign an implementation agreement to develop the 'pollution free' Coal, Cement and Clinker Terminal (CCCT) worth US$175 million at Port Qasim.

Fauji Cement's new plant

Fauji Cement Co. Ltd is installing the country's biggest cement plant, with a capacity of 7560 tpd of clinker, in parallel with the existing production line in Jhang-Bahtar. This will also increase Fauji Cement's annual installed capacity by almost three times - from its existing 1.165 million t to 3.27 million t of cement.

This cement plant will be the first in Pakistan by Polysius. Prior to this, FLSmidth has held a major share in commissioning cement plants in the country. Fauji Cement's new plant is scheduled to start production by May 2010. The company has taken the initiative to spend Rs.320 million on Pakistan's first refuse derived fuel (RDF) processing plant. Hundreds of tonnes of garbage, collected on a daily basis from nearby cities Rawalpindi and Islamabad, will be converted into fuel for burning in the kiln. The RDF plant will have the capacity to produce 12 tph of processed RDF (2.75 t of processed RDF replaces 1 t of coal). The company plans to enhance this capacity to 36 tph in the future, incurring a saving of 250 – 260 tpd of coal. In addition to coal saving, the use of RDF plant will lower greenhouse gas emissions and will provide fertilizer as a byproduct.

These ambitious large capacity expansion programmes are designed to meet the increasing export deficit in the region. The success of the cement sector depends on exports, its profitability from depressed local prices and cost appreciation.

Maple Leaf cement plant is one of the largest producers with 6700 tpd clinker capacity.

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