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STOCK INSIGHT GRAPHITE INDIA

Anchored to steel

Graphite electrode is a product whose fortunes are linked to growth in steel manufacturing. Buy stocks of the leading manufacturer only on dips



Graphite India Limited (GIL) is India's leading producer of graphite electrodes and is one of the largest globally. The company accounts for approximately 6.5 per cent of global electrode capacity. It manufactures the full range of graphite electrodes but focuses mostly on the higher margin, large diameter, ultra-high power (UHP) electrodes. Approximately 85 per cent of the company's total capacity is currently in UHP electrodes. The company's manufacturing facilities are located at Durgapur (34 kilo tonne), Bangalore (13KT), Nashik (13KT) and Nurnberg, Germany (18KT). GIL also has facilities designed for the manufacture of calcined petroleum coke (30 KT), impervious graphite equipment, and glass reinforced plastic pipes and tanks. It has an installed capacity of 33 MW for power generation through hydel and multi-fuel routes.

Sectoral outlook

Graphite electrodes are used in electric arc furnace (EAF) based steel mills for conducting current. It is a consumable item for the steel industry. Its demand is primarily linked with the global production of steel using EAFs. The global graphite electrode industry

operated at approximately 50 per cent of its installed capacity in FY10 on account of weak demand, reduced steel production, and de-stocking throughout the value chain of the industry (as a result of the global recession). While the global economy is recovering from the crisis, demand from the steel-using sectors remains weak.

However, the share of steel production using EAFs has increased over the last two decades from 26 per cent to about 32 per cent globally. The share of EAF-based production is expected to grow further in the years to come due to its inherent positive characteristics: it is environment friendly, pollutes less, requires less capital, and the time required for commissioning EAF-based plants is shorter.

Further, according to Rahul Dholam, senior research analyst at Unicon Securities, "Steel demand is expected to increase from the current 64 MTPA to 128 MTPA in the next few years, and increase to 200 MTPA by 2020. Over the next couple of years, the share of steel production via the EAF route is expected to remain at around 32 per cent. Hence, we feel that the demand for graphite electrodes could double in the next few years."

Strengths

Labour cost advantage. GIL has a strong labour cost advantage compared to its global peers, as the other companies have their plants in locations where labour costs are significantly higher compared to India. The largest global player, SGL Carbon SE, has plants located mainly across Europe and North America. GrafTech Ltd, the world's second-largest player, has plants in France, Spain, South Africa, Brazil and Mexico. In a recent report, Jai Sharda, analyst at Angel Broking, says that historically GIL has passed on a part of this advantage to gain market share. But with gains in market share expected to slow down, it expected that GIL will retain a larger part of this cost advantage and thereby improve its margins over historical levels.

High entry barriers. The global graphite electrodes industry is highly consolidated. The top five global players account for over 75 per cent of graphite elec-