



“Globus Spirits Limited Q1 FY-2014 Earnings Conference Call”

August 12, 2013



MANAGEMENT: **MR. AJAY KUMAR SWARUP – MANAGING DIRECTOR,
GLOBUS SPIRITS LIMITED**
**MR. SHEKHAR SWARUP – EXECUTIVE DIRECTOR, GLOBUS
SPIRITS LIMITED**
**DR. BHASKAR ROY – DIRECTOR & CFO, GLOBUS SPIRITS
LIMITED**
**MR CHALAM SURAMPUDI. BUSINESS HEAD – PROJECTS
AND SUPPLY CHAIN**
**MR. PARITOSH BHANDARI – HEAD, SALES & MARKETING,
GLOBUS SPIRITS**

MODERATOR: **MR. NIKHIL VORA – MANAGING DIRECTOR, IDFC
SECURITIES**



*Globus Spirits Limited
August 12, 2013*

Moderator

Ladies and gentlemen good day and welcome to the Q1 FY14 Earnings Conference Call of Globus Spirits hosted by IDFC Securities. As a reminder, all participants' line will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during this Conference call please signal an operator by pressing * followed by 0 on your Touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Nikhil Vora of IDFC Securities. Thank you and over to you, Mr. Vora.

Nikhil Vora

Welcome you all to the Q1 FY14 earnings conference call for Globus Spirits. We have with us the management team of Globus represented by Mr Ajay Swarup – Managing Director; Mr Shekhar Swarup – Executive Director; and Dr. Bhaskar Roy – Director & CFO. I will hand it over to Ajay to make the opening remarks and then we will open the floor for Q&A. Over to you, Ajay.

Ajay Swarup

Good afternoon everyone. It is a pleasure to welcome you in our Q1 FY14 Earnings Call. I will walk you through our achievements in this period following which our CFO – Dr. Roy will take you through the financial results post which the floor will be opened for Q&A. We have with us the entire top management team of the company to field questions which you may have.

This quarter has been encouraging for us as we have sustained our operational margins overcoming many challenges. This included industry-wide cost rises, pushed by steep rise in grain prices, new changes in IMIL packaging and the subdued economic environment. There were two positives in our favor. First, there was increase in realizations in all the segments we operate in the spirits value chain. The second was improvement in alcohol recoveries per kg of grain, which is our basic raw material. This has been a result of our continuous research & development initiatives and, of course, our investments in cutting edge technologies. The credit for this goes to our entire team who made it possible for us to be now the industry's most efficient grain based distillery.

The longer term benefit is that we have been able to create a competitive cost advantage of manufacturing high quality grain based alcohol at costs which are competitive across various raw materials available for making alcohol. We aim to strengthen our position, both in the domestic and export markets, while improving our overall profitability.

Our top line growth has been boosted by manufacturing businesses. Our franchise bottling business, which is a proxy play on the IMFL industry, showed strong traction largely driven by our contracts with United Spirits Limited and Jagatjit Industries Limited.

We are today suppliers to India's top 3 IMFL companies; a testimony to our high quality products and our reputation as a credible and established alcohol company. Our overall bulk



*Globus Spirits Limited
August 12, 2013*

production increased by one-fifth this quarter as we operated our new multi pressure distillation technology based capacities at high utilizations. This resulted in a 22% year-on-year growth in our bulk sales segment. In IMIL, we benefitted from price increases in all our states. Our Rajasthan market continued on its growth path. Our IMIL brand Nimboo continues to perform well across markets. In Haryana, we experienced a period of further consolidation.

Haryana IMIL market has both white and colored spirit categories and the colored category is cluttered by orange flavored generics. To break this clutter, and to gain market share in this colored segment, this quarter, we launched India's first mixed fruit IMIL blend by the name of Goldee. The brand is a well researched product that has shown strong acceptance in the focus groups. We are hopeful that Goldee will emerge as our second flagship IMIL brand. Our marketing & sales teams are working tirelessly to make this happen, which we believe will be a major step forward for the company.

In IMFL, our focus on three core profitable brands helped us increase our realizations. Simultaneously, we have exited all the markets which were not showing a positive contribution in the IMFL business. Our first CSD orders have come in and are currently under execution. We are hopeful of seeing good traction in CSD by the end of this year.

On the whole, our business has emerged resilient in the current economic slowdown. Going forward, as the economy revives and we expand geographically, we are hopeful of returning to double digit growth and higher returns. Our Bihar project is moving as planned and we should see operations starting in FY2015-16.

Our company is continuously implementing initiatives to increase productivity, quality and efficiency in alcohol manufacturing as well as in the by-products chain. We see opportunities in export for our high quality products. On the cost front, grain prices have now stabilized and we should see improvement in margins going forward.

I would now like to handover to Dr. Roy, our CFO, for the overview on our financial performance.

Dr Bhaskar Roy

I will share our financial highlights, after which, we will open the floor for questions.

For Quarter 1 FY14, the total operating income was Rs. 1,396 million, an increase of 6.4% year-to-year. The EBITDA was Rs. 198 million, an increase of 5.3% year-to-year. The PAT was at Rs. 92 million. EBITDA margin was maintained at 14.2%. We have achieved stability in EBITDA margin in spite of 22% year-to-year increase in grain prices and new IMIL packaging guidelines that came along with the price hikes. This has been possible as we were able to improve realizations across all our segments.



Globus Spirits Limited
August 12, 2013

On the cost side, our R&D initiatives and operating of new multi pressure distillation plants helped us improve our grain recoveries by 8.4% year-to-year. So overall the EBITDA margin was insulated as our raw material cost as percentage of sales came down to 61.3% in that quarter as compared to 63.6% in Quarter 1 FY13. The PAT margin was 6.6% for the quarter on account of the increased depreciation and interest cost due to recently increased capacity.

I will now share the segment wise details. This quarter, we sold 2.2 million cases of IMIL with average net realization of Rs. 287 per case, an increase of 8.5% year-to-year in realization. In IMFL, we sold 33,000 cases with 10% year-to-year increase in the average net realizations. The combined net sales from these two consumer businesses was Rs. 629 million for the quarter. In franchise IMFL, the aggregate volume for the quarter was 5,58,000 cases, an increase of 39% year-to-year by volumes. Our bottling sales case increased 8.9% year-to-year. Our bulk alcohol sales increased 22% year-to-year to reach 12.4 million bulk liters with 5% year-to-year increase in realization. This was mainly due to 42.2 million beer capacity added in for FY13 at the existing locations.

The total revenues from manufacturing were Rs. 653 million this quarter, an increase of 31% year-to-year. This concludes my update. Thank you once again for joining us on the conference call. We will be happy to answer any questions that you may have now.

Moderator	Thank you very much, sir. Participants we will now begin with the Question & Answer Session. The first question is from Vishal Gajwani from Birla Sun Life Insurance. Please go ahead.
Vishal Gajwani	Sir, if you can just highlight for the full year what kind of volumes you are expecting and what kind of margins should be expected?
Dr. Bhaskar Roy	Volumes, you want the segment wise?
Vishal Gajwani	Right, segment wise.
Dr. Bhaskar Roy	The volumes will be similar to what we have done in quarter one, if not more. The new capacities have stabilized due to the manufacturing (bulk) business.. So the manufacturing (bulk and franchise) will be more than the consumer segment. We are hopeful of maintaining margins at last quarter's level.
Vishal Gajwani	And since FY14 is a year of state elections and May FY15, early FY15 there will be central elections so can we expect some kind of volume growth just because of that?
Shekhar Swarup	There will be no volume growth which can be attributed to elections. Certainly during the election period there are a few dry days which could hamper, in the very short term, some sales but there is no growth attributable to elections per se.



Globus Spirits Limited
August 12, 2013

- Vishal Gajwani** And if you can just take me through the various brands. I believe Nimboo is there and then Goldee that you have launched. So, what kind of revenue contribution comes from each one of the brands and what kind of growth you are looking at in these brands?
- Shekhar Swarup** Nimboo is our flagship IMIL brand which operates in the clear color segment in Haryana. Goldee is a new brand which we have put in to the market. So, at present, the revenue shares would be very small. Besides that, we have in IMFL County Club Whisky, Hannibal Rum which are in the regular price point at about Rs. 200 MRP for a 750 ml bottle. We have a semi-premium brand in brandy in South India by the name of French Castle. In terms of revenue shares, Dr. Roy would you like to answer that?
- Dr. Bhaskar Roy** 49% is our consumer business and manufacturing is 51% at this moment.
- Vishal Gajwani** And within that, if you can just give a breakup - brand wise – of the revenue contribution within consumers?
- Shekhar Swarup** If you see in IMIL, the price point is same. Today Nimboo is contributing the highest percentage in IMIL, but there is no difference in contribution as the price point is same. So, just to give you an idea, Nimboo would be about 50% of IMIL volumes and the IMFL brands County Club and Hannibal would be about 70% to 75% of IMFL volumes.
- Vishal Gajwani** No, but Nimboo you said is 50%?
- Shekhar Swarup** 50% IMIL revenues and the other two brands which are IMFL would be 70% to 75% of IMFL revenues.
- Vishal Gajwani** And what is the slab between IMFL and IMIL?
- Shekhar Swarup** Largely our consumer business is IMIL. The number for that is about 90% would be IMIL and the balance would be IMFL.
- Vishal Gajwani** The growth trajectory in both these IMIL and IMFL if you can just through some light on that?
- Dr. Bhaskar Roy** In the IMFL segment we have changed the strategy ie we have discontinued the cheap brands which were making losses and we are now concentrating mainly on the regular brands and the brands above that. So the volumes have decreased in the IMFL but the margins have improved, number one. Number two, in the IMIL segment, we are concentrating our position in the existing territories of Haryana, Delhi and Rajasthan where we are operating at present and also exploring newer markets like Maharashtra and the eastern parts for future growth.
- Vishal Gajwani** And what kind of growth expectation is there for the IMIL portfolio?



Globus Spirits Limited
August 12, 2013

- Shekhar Swarup** Actually, in IMIL, we will grow with the markets growing at 4-5%. Whatever rate the market is growing at, we will grow at that speed. But, as soon we enter in a new territories, as our base will be zero so growth will be naturally higher which we are trying to do as fast as possible.
- Vishal Gajwani** Organic growth will be 5% while your new geography expansion will add to the growth?
- Shekhar Swarup** Yes.
- Vishal Gajwani** What kind of new geography expansion growth can we look at for FY14?
- Shekhar Swarup** We have kick started projects in East India which have a consumption growing in excess of 20% in each state. In the quarter before last we have raised funds from Franklin Templeton for that project and we are hoping to break ground within this financial year and have the project commissioned in FY16.
- Moderator** Thank you. We have the next question is from the line of Dhiraj Sachdev from HSBC. Please go ahead.
- Dhiraj Sachdev** If you can just give us a break up of your 14% EBITDA margins between IMFL franchise and bulk sales?
- Shekhar Swarup** Actually giving a segment wise EBITDA margin is very difficult because, what has happened is, being a producer of alcohol ourselves we first produce the alcohol and then this alcohol is transferred to the bottle segment, etc. So, it is difficult. But we can say that the overall EBITDA we are maintaining is at about 14%. Higher contribution with a higher EBITDA margin in IMIL and lesser than that is yielded with the bulk.
- Dhiraj Sachdev** And if you can just roughly touch up on what is the difference in margins between contract manufacturing IMFL and your own IMIL?
- Dr. Bhaskar Roy** In contract manufacturing of IMFL, there are two points of generating EBITDA. One point is sale of alcohol where the margin is equivalent to the margin in bulk alcohol which we are selling outside. The other is the fixed margin per case which is the bottling income we have. And in own IMFL, the margin is higher.
- Shekhar Swarup** The question was for IMIL, the margin in own IMIL is significantly higher than the margin in franchise manufacturing.
- Dhiraj Sachdev** Sir, if you can just tell me is it 4% to 5% higher than the contract manufacturing, just to get an idea?
- Shekhar Swarup** It would be above 5% points higher.



Globus Spirits Limited
August 12, 2013

Dhiraj Sachdev

So then, from the capital efficiency point of view it is IMIL that is obviously more capital efficient as a business compared to contract manufacturing?

Shekhar Swarup

Yes, however our business needs to be looked at in its entirety because any standalone vertical would not be as profitable as it is today if the others were not coexisting with it. We are able to get higher return on capital because of the 360 degree model. If we remove franchise manufacturing from this piece we will not get the efficiencies we have today.

Dhiraj Sachdev

And the next question I know it is very difficult to estimate the grain prices but the inflation impact of 20% to 22% on grain how you combating it and what is the outlook there?

Shekhar Swarup

We have been combating these grain price pressures by increasing the value-add on by-products as well as increasing recoveries from grain. In quarter one, we have increased our efficiencies significantly and therefore our raw material as apportioned to sales has come down from 65% to 61%.

Dhiraj Sachdev

Could you comment on the grain prices for the rest of the year?

Chalam Surampudi

Yes. The grain prices are definitely a challenge today. They are going up and there are several reasons why they are going up. One is, of course, the opening up of exports of various grades of grains especially non-basmati grain which has started getting exported about 2 to 3 years ago and it has taken up momentum and now that is actually having an impact on the prices. Then, of course, there is the availability of grains and the increase in demand as well of the variety of grains that we purchase. All of these have put pressure on the prices of grain, but what we are doing in order to combat that is to have more frequent negotiations with the supplier and we are also looking a little at sources which are a little further away and trying to see if we can somehow obtain price reductions and sort of offset the transportation cost that will obviously be higher if we buy from far field. All of these measures are actually bringing us some amount of relief, we are able to keep the prices steady but then there are rumors coming in from the market players that prices are actually going to go up in the next couple of months because of shortages that are expected as the new season is still a couple of months away. So that is where they are at right now and how we are going to combat is to try and get some new sources and also put pressure on prices from the existing sources.

Moderator

Thank you. We will take the next question from the line of Ms Swati.

Swati Nangalia

My question is pertaining to the mix of our business so in this quarter - we have seen the contribution of the consumer segment come down significantly on a Y-o-Y basis and manufacturing has trended up, so is this the mix we would like to continue with going forward?



Globus Spirits Limited
August 12, 2013

Shekhar Swarup

It is actually a very crucial question for us. As you are aware, we look at our business, like I said earlier, from a 360 degree point of view where we first manufacture the alcohol and then try to maximize allocation of that alcohol to higher margin consumer businesses. A few years ago when we did the IPO and raised funds to put up our initial projects we were actually consuming more alcohol in our higher value added businesses than we were producing. The reason this has gradually come down from like I said over 100% to about 50% today because of increasing capacities. In the last quarter, we also saw a decrease in the consumer business because of focus on higher value-added products as well as contraction of Haryana key market. But, going forward, we want to maintain a healthy mix of manufacturing as well as consumer. It is very difficult for me to say whether 50% is that healthy mix but certainly our priority is to maximize the allocation to consumer businesses.

Swati Nangalia

And how do we intend to do that, because, given the fact that the consumer segment is definitely more profitable than the manufacturing segment, do we have a road map on any key brands or especially in the IMFL or segment which you are trying to launch in the near future?

Shekhar Swarup

Certainly, IMFL and IMIL both are extremely important for us. Our focus on creating quality brands in the IMIL space has made us stand out in the market. Nimboo was one such example. In the last quarter, our marketing department has created a new brand for the IMIL division called Goldee which is the country's first mix fruit beverage for the Haryana market. I will defer to Paritosh to give you a little more insight on that but before that on IMFL like we said earlier we are focusing on higher value added brand in the Goldee our position of cheap brands in IMFL and going forward we will be putting in place premium products with international alliances and even without international alliances. Paritosh, could you share a little bit about Goldee and how are plan to make that successful?

Paritosh

So especially in Haryana market what we realized was that the contribution from the colored segment was very high at about 70% to 75% and the idea was to have a strong player like we have Nimboo for the white segment or the clear segment. We wanted to create a new brand within the dark or the colored segment as well and that is where researched and came up with this whole idea of coming up with innovation as far as blend and packaging was concerned. That is where we developed this new blend not in the regular offerings like orange, etc., but with a mix of fruits and the initial acceptance as we are sampling in the trade and among the consumers is very high, almost resulting in about 50% to 60% conversion at the consumer level. So that is where Goldee is pitching in and we continuously strive to sort of develop a few more blends so that we capture our share in the color segment as well. Similarly, in IMFL, Shekhar just touched upon development of premium business in from now and that is where we are looking at alliances across the globe to come up with offerings in the premium and super premium segments.

Swati Nangalia

Just lastly I just wanted your take on the changes which the Indian alcohol industry is undergoing currently. We have seen Diageo take a stake in United Spirits and also Pernod has



Globus Spirits Limited
August 12, 2013

done reasonably well in the Indian market. So now with Diageo and Pernod controlling almost 60% of the volumes, how would we read this impacting someone like us in terms of the markets which we operate in and for the industry in general?

Shekhar Swarup

Well, the IMFL markets which is what you are referring to which is 50% of the spirits industry has always been controlled by two players. In the past, USL had over 60% market share and then gradually some of the other players came up. So in terms of market structure as of today it would not change much, however, it would be interesting to learn about the strategies of these companies and the portfolio of brands going forward. We are expecting that Diageo and Pernod will continue to focus on higher value added brands and perhaps the low value added brands may not interest them as much as it did the earlier management. That could open up some interesting spaces for higher efficiency players such as ourselves to create niches for themselves in the market. That is one point. The other point is that as these multinational companies are coming in we have seen from their global practices that they like to manufacture less and market more which means that player such as ourselves which are integrated 360 degree players will perhaps have more importance in the market as their capacities would be at a premium coupled with the demand for fuel ethanol as our molasses counterparts dedicated more capacity for fuel ethanol there is less beverage alcohol available in the market driving up prices for our alcohol. According to me, these are the few changes that are taking place in the market. It is difficult to say exactly how it will pan out but that is what my expectation is.

Moderator

Thank you. As there are no further questions from the participants I would now like to hand the floor back to Mr. Nikhil Vora for closing comments. Over to you, sir.

Nikhil Vora

Thanks all the participants for being on the call and the management team there. Any closing remarks Ajay, you can make that?

Shekhar Swarup

Thank you very much for your time. Hope to see you again at the next earning calls.

Moderator

Thank you, sir. Ladies and gentlemen on behalf of IDFC Securities that concludes this conference call. Thank you for joining us, you may now disconnect your lines.