Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)		✓	
Right Valuation (RV)		✓	

\+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

Company details

Market cap:	Rs. 2,119 cr
52-week high/low:	Rs. 1,760 / 700
NSE volume: (No of shares)	1.3 lakh
BSE code:	533104
NSE code:	GLOBUSSPR
Free float: (No of shares)	1.4 cr

Shareholding (%)

Promoters	51.0
FII	6.9
DII	1.7
Others	40.4

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	-10.7	-18.1	-40.2	-36.1
Relative to Sensex	-16.6	-20.8	-54.1	-38.0

Sharekhan Research, Bloomberg

Viewpoint

Result Update

Globus Spirits Ltd

Weak Q2; near term outlook bleak

Consumer goods		Sharekhan code: GLOBUSSPR	
Reco/View: Neutral	↔	CMP: Rs. 737	Upside potential: 12% ↓

↑ Upgrade ↔ Maintain ↓ Downgrade

Summary

- Globus Spirits Q2FY2023 performance was weak, affected by 10% decline in revenues of the consumer business (due to market share loss in Haryana and policy change in Rajasthan impacting value plus volumes) and sharp decline in the EBIDTA margins led by higher input and fuel cost.
- Capacity expansion will drive strong growth in the bulk alcohol business, while in the consumer business, Haryana will see a revival in sales volume while Rajasthan sales volume will take time to revive. Revenue growth will remain in double-digit largely driven by capacity expansion.
- With softening of raw material prices and correction in the fuel prices, the company expects EBIDTA margins to reach 15% by Q4FY2023. It will stay at around 16-18% in FY2024 (GSL lowered its guidance of 20%).
- The stock is currently trading at 13.5x/9.4x its FY2023E/FY2024E EPS. In view of near-term margin headwinds, we retain our Neutral stance with an upside of 12%.

Globus Spirits Limited (GSL) registered yet another quarter of disappointing performance in Q2FY2023, with PAT declining by 58% y-o-y to Rs. 22 crore due to a sharp decline in the EBIDTA margins to 9.4% in Q2FY2023 from 23.0% in Q2FY2022. Net revenues grew by 26% y-o-y (decreased by 3% q-o-q) to Rs. 480.3 crore largely driven by sharp 84% y-o-y growth in the bulk alcohol revenue to Rs. 317.2 crore led by enhanced capacities and improve realisation (capacity utilisation at new plant is around 95%). Consumer business revenues decreased by 10% y-o-y to Rs. 163.1 crore. Gross margins fell by 729 bps y-o-y to 41.1% mainly on account of higher input cost and change in the mix. However, the same stood stable on q-o-q basis. Operating profit decreased by 49% y-o-y to Rs. 44.9 crore. In H1FY2023, revenue grew by 29.6% y-o-y to Rs. 975.7 crore, PAT declined by 45.1% y-o-y to Rs. 59.4 crore, while OPM contracted by 131 bps y-o-y to 11.6%.

Key positives

- Enhanced capacity led to bulk alcohol sales volume growing to 4.33 crore litre; volume increased by 62% y-o-y.
- Average realisation of bulk alcohol grew by 14% y-o-y to Rs. 58.5 per litre on account of ethanol price hike and better ENA realisation.
- Gross margins stood flat at 41% on a q-o-q basis.

Key negatives

- EBIDTA margins decreased to 9.4% from 23.0% in Q2FY2022, mainly on account of lower operating leverage due to a lower share of high-margin consumer business (34% of sales) and higher cost of power and furl during the quarter.
- Consumer business revenues were down by 10%; temporary softening of market share in Haryana due to temporary focus on achieving profitable sales.

Management Commentary

- Jharkhand facility of 140 KLPD started operating in September 2022; 60 KLPD expansion in West Bengal & Jharkhand is expected to be operational in Q1FY2024, while expansion in Odisha and Uttar Pradesh is at the initial stages of land acquisition. GSL expects total capacity to increase from 760 KLPD currently to 944 KLPD by the start of FY2024. Orissa and Uttar Pradesh green field projects of 200 KLPD each will be underway soon with capacity expansion to 1,344 KLPD (will increase to 41 crore litres in 3-4 years).
- To mitigate impact of the increase in raw material (broken rice) costs, GSL started procuring rice from the Food Corporation of India (FCI), which fetches an incremental ethanol realisation of ~Rs. 3 per litre (Ethanol from surplus rice vs ethanol from damaged food grain). For FY2023, ~40% of raw material consumption will be done from FCI.
- Further, backward integration for PET bottles coal linkages with Coal India for the supply of coal in the eastern part of India (will lead to a reduction in coal procurement cost by ~20%), price hikes in key markets, reduction in the key input prices and fuel prices will help EBIDTA margins to recover to 15% in Q4FY2023. The same is expected to remain at 16-18% in FY2024. Stable input prices and higher realisation due to a better mix will help the margins to improve in the medium term.
- Consumer business sales were impacted by an increased focus on profitable sale in Haryana leading to a temporary loss in the market share in the state. However, the other players have also taken price action, and hence Haryana state sales volume is expected to improve in the coming quarters. In Rajasthan, there was change in the business mix due to the policy change resulting in 25% growth in value segment while value plus segment was down by 35% y-o-y. It will take some time for sales volume of the value plus segment to revive in the near term.

Revision in estimates – We have lowered our estimates for FY2023/24 to factor in lower than earlier expected OPM due to the impact of higher fuel costs and input costs on margins. The company has reduced its OPM guidance to 16-18% from 18-20% earlier as a mix of manufacturing, and consumer businesses will remain at 60:40. We have introduced FY2025 earnings estimates through this note.

Our Call

View – Retain neutral stance with 12% upside: In the past few quarters, performance was affected by a sharp decline in the OPM due to a sharp increase in the input costs and a change in the revenue mix. The management has taken key initiatives to reduce stress on margins. However, the benefits of key initiatives and the expected rise in realisations would flow in from FY2024. The performance will be subdued in the near term due to lower profitability. Thus, in view of near-term margin headwinds, we retain our neutral stance on the stock with a potential upside of 12%. The stock trades at 13.5x/9.4x its FY2023/24E earnings.

Key Risks

Any quick and significant improvement in the margins will drive strong earnings growth in the quarters ahead, which will act as a key risk to our rating on the stock.

Valuation (Consolidated) Rs cr

Particulars	FY21	FY22	FY23E	FY24E	FY25E
Revenue	1,231	1,579	1,999	2,316	2,673
OPM (%)	20.7	20.8	13.0	16.0	17.0
Adjusted PAT	144	187	157	225	284
Adjusted EPS (Rs.)	50.0	65.0	54.5	78.1	98.5
P/E (x)	14.7	11.3	13.5	9.4	7.5
P/B (x)	3.6	2.7	2.3	1.9	1.5
EV/EBIDTA (x)	8.6	6.7	8.5	5.9	4.4
RoNW (%)	24.4	24.2	17.0	19.7	20.0
RoCE (%)	26.7	28.0	18.0	22.8	23.8

Source: Company; Sharekhan estimates

Revenue growth at 25.7% y-o-y; profitability impacted

Consolidated revenues grew by 25.7% y-o-y to Rs. 480.3 crore driven by 57.3% y-o-y growth in the manufacturing business, while consumer business revenues declined by 9.7% y-o-y to Rs. 163 crore. Bulk alcohol business sales volume grew by 62% y-o-y to 43.33 mn litres in Q2FY2023. Consumer business sales volume declined by 17% y-o-y to 3.16 mn cases during the quarter. High input costs and an unfavourable mix led to sharp 729 bps y-o-y decline in the gross margins to 41.1%. Gross margins were maintained on a sequential basis due to higher realisation in the bulk alcohol and consumer segment. OPM decreased to 9.4% in Q2FY2023 from 23.0% in Q2FY2022, impacted by high power and fuel costs, softening of market share in Haryana and a change of business mix in Rajasthan. Operating profit decreased by 48.8% y-o-y to Rs. 44.9 crore. Adjusted PAT declined by 57.9% y-o-y to Rs. 22.1 crore. In H1FY2023, revenue grew by 29.6% y-o-y to Rs. 975.7 crore, PAT declined by 45.1% y-o-y to Rs. 59.4 crore, while OPM contracted by 131 bps y-o-y to 11.6%.

Strong double-digit growth in the manufacturing business

The manufacturing business registered a y-o-y growth of 57.3% y-o-y in Q2FY2023 to Rs. 317.2 crore led by enhanced capacities and improved realisations. Bulk alcohol business sales volume grew by 62% y-o-y and 6% q-o-q to 43.33 mn litres in Q2FY2023, backed by expanded capacity (West Bengal capacity addition in Q4FY22). The average realisation grew by 14% y-o-y and 2% q-o-q to Rs. 58.5 per litre in Q2FY2023 on account of Ethanol price hike and better ENA realization. Capacity utilisation came in at ~90% in H1FY23 with an expanded capacity.

Weak Q2 for consumer business; recovery expected in H2

GSL's consumer business (largely IMIL sales) declined by 9.7% y-o-y to Rs. 163 crore in Q2FY2023 impacted by lower volume during the quarter. Sales volume in Q2FY2023 came in at 3.16 mn cases (lower by 17% y-o-y). Premium segment revenue grew by 297% y-o-y to Rs. 44 million in Q2FY2023 and is expected to continue the growth momentum. The management has indicated that full-year revenue contribution of the premium segment would grow to 6% of the total consumer segment, from 3% currently. New market launches are expected in the premium segment in H2FY2023. In Haryana, increased focus on profitable sales led to a temporary softening of market share in Q2FY23 and increased margin by 26 per case. Management has stated that the strategy has started to bear fruit, and market share is building up. In Rajasthan, GSL witnessed change in business mix due to policy change. The value segment market grew by 25% y-o-y, while the value plus segment market declined by 35% y-o-y in Q2FY2023. GSL's market share is up by 2% and 8% in value and value plus segments, respectively, in Q2FY2023. Overall, consumer business volume is up by 4% y-o-y, from 5.3 mn cases in H1FY22 to 5.5 mn cases in H1FY23.

Capacity expansion plans on track

GSL currently has various capacity expansion projects under progress/competition. The new greenfield capacity addition of 140 KLPD with bottling plants at Jharkhand commenced commercial production in August 2022. The plant is likely to operate at optimum utilisation in Q2FY2023. The company has started work on enhancing the capacity by 60 KLPD each at West Bengal and Jharkhand, with both plants likely to be commissioned by Q4FY2023. In Bihar, an additional capacity of 19 KLPD is being set up, which is expected to be operational by Q4FY2023. In Odisha and UP, the company is working towards taking the necessary approvals. Total capacity is expected to increase from 760 KLPD currently to 1,344 KLPD in the medium term. As per the management, all projects will be funded through internal accruals.

Results (Consolidated) | **Rs cr**

Particulars	Q2FY23	Q2FY22	Y-o-Y %	Q1FY23	Q-o-Q %
Net sales	**480.3**	**382.2**	**25.7**	**495.4**	**-3.1**
Material cost	282.9	197.2	43.4	292.1	-3.1
Employee cost	13.7	10.7	27.9	14.2	-3.1
Other expenses	138.8	86.5	60.5	120.6	15.1
Total operating expenses	435.4	294.4	47.9	426.8	2.0
Operating profit	**44.9**	**87.8**	**-48.8**	**68.6**	**-34.5**
Other income	2.1	1.6	34.0	1.7	22.9
Interest expense	2.5	2.4	5.1	2.2	14.0
Depreciation	12.9	10.4	24.0	12.5	3.5
Profit before tax	**31.6**	**76.5**	**-58.7**	**55.6**	**-43.2**
Tax	9.4	24.0	-60.7	18.3	-48.5
Adjusted PAT (before MI)	22.1	52.5	-57.8	37.3	-40.6
Minority interest (MI)	0.0	0.1	-100.0	0.0	-
Reported PAT	**22.1**	**52.6**	**-57.9**	**37.3**	**-40.6**
EPS (Rs.)	7.7	18.2	-57.8	12.9	-40.6
			bps		**bps**
GPM (%)	41.1	48.4	-729	41.0	6
OPM (%)	9.4	23.0	-	13.8	-449
NPM (%)	4.6	13.7	-913	7.5	-291
Tax rate (%)	29.9	31.4	-149	33.0	-308

Source: Company; Sharekhan Research

Segmental performance

Particulars	Q2FY23	Q2FY22	Y-o-Y %	Q1FY23	Q-o-Q %
Consumer business	163.0	180.6	-9.7	194.0	-16.0
Manufacturing (bulk) business	253.4	137.9	83.8	234.3	8.2
Manufacturing (other) business	63.8	63.7	0.1	67.9	-6.0
Net revenue from operations	**480.3**	**382.2**	**25.7**	**495.4**	**-3.1**

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector Outlook – Structural change in the alcohol industry

Indian Made Indian Liquor (IMIL) is evolving from a restricted quota-based, commoditised market to a consumer-driven brand-based industry. The main attractiveness of this market lies in its sizeable base, comprising SEC-D below which could translate into ~40% of the total population (excluding the Below Poverty Line). Growth in this segment is expected to be driven by a growing consumer base, rising rural incomes, and consumption, conversion from illicit/toddy to IMIL with increasing awareness about health and quality, conducive regulatory policies, and population growth. In the short run, the IMIL industry could benefit from lower discretionary incomes, which would push up demand for lower-priced liquor. The government is targeting to achieve a 20% blending of ethanol by 2025, which would result in higher demand for grain-based molasses in the coming years.

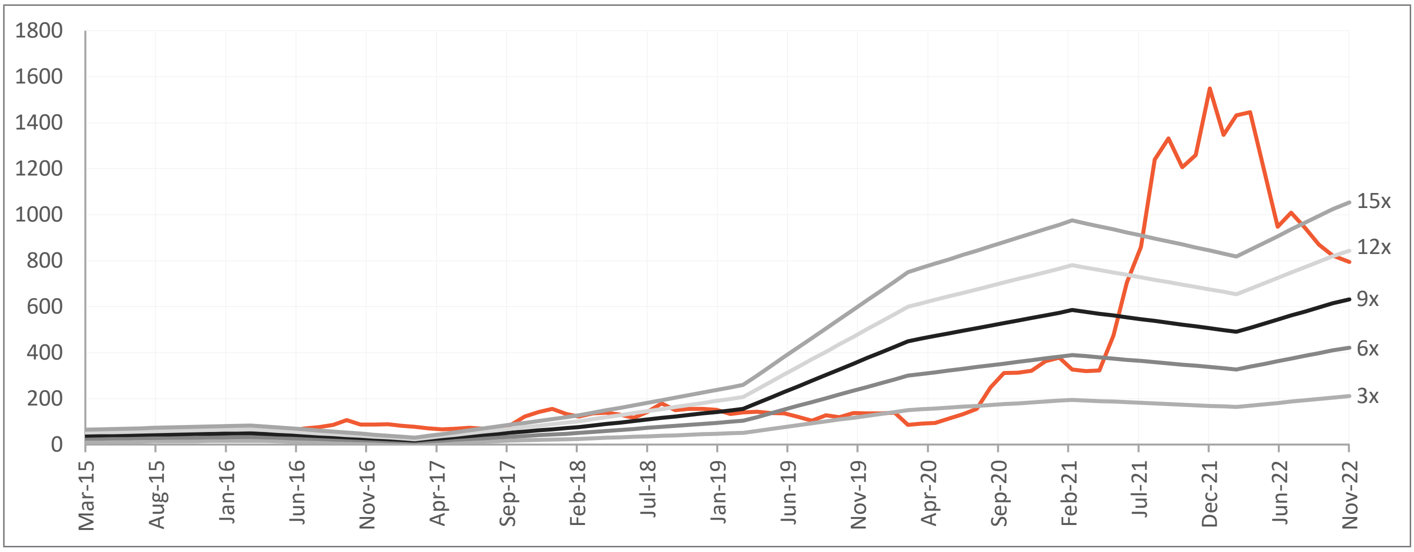
■ Company outlook – Margins to remain under pressure in the near term

Raw material price inflation, increase in fuel prices and change in the mix will continue to pressurise the margins in the near term. We expect OPM to reduce to 12-13% in FY2023 and will improve to 16% by FY2024 (lower than earlier expectation of 18-20%). Earnings to decline in FY2023 due to lower margins while growing in strong double digits due to improvement in the margins. Around 40% of the expanded capacity (of 1,090 KLPD) will be utilised for manufacturing ethanol in long run.. The company plans to double its capacity over the next 3-4 years from 760 KLPD currently to 1,344 KLPD. The contribution of the consumer business is expected to stand at 40% in the near term.

■ Valuation – Retain Neutral stance with 12% upside

In the past few quarters, performance was affected by a sharp decline in the OPM due to a sharp increase in the input costs and a change in the revenue mix. The management has taken key initiatives to reduce stress on margins. However, the benefits of key initiatives and the expected rise in realisations would flow in from FY2024. The performance will be subdued in the near term due to lower profitability. Thus, in view of near-term margin headwinds, we retain our neutral stance on the stock with a potential upside of 12%. The stock trades at 13.5x/9.4x its FY2023/24E earnings.

One-year forward P/E (x) band



Source: Company, Sharekhan Research

Peer Comparison

Particulars	P/E (x)			EV/EBITDA (x)			RoCE (%)		
	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
United Spirits	72.4	58.8	53.9	44.1	40.9	35.5	25.4	26.6	29.7
Radico Khaitan	49.6	49.3	36.3	32.4	31.8	23.3	15.1	13.3	17.1
Globus Spirits	11.3	13.5	9.4	6.7	8.5	5.9	28.0	18.0	22.8

Source: Company, Sharekhan estimates

About company

Established in 1992, GSL is one of the leading players in the Indian alcoholic beverages industry. The company manufactures, markets, and sells Indian Made Indian Liquor (IMIL), Indian Made Foreign Liquor (IMFL), bulk alcohol, and contract bottling for established IMFL brands. GSL's manufacturing business segment contributes ~59% to revenue and comprises bulk spirits, franchisee bottling, and by-products, whereas the consumer business segment contributes ~41% to revenue and comprises the value segment and premium segment. GSL is one of the largest and most efficient grain-based distilleries in India with a capacity of 195 million litres.

Investment theme

GSL will be one of the key beneficiaries of the change in the government's ethanol policy, with 50% of ethanol blending expected to happen through grain based. Around 75% of expanded capacity (420 KLPD) will be used to manufacture ethanol. Consumer business's (IMIL) contribution has increased to 41% versus 35% in recent years, with 2x higher margins than the bulk alcohol business. With increased sustainable demand for ethanol and scale-up in the consumer business, GSL's earnings are expected to grow in strong double digits in FY2024. However, in the near term, the margins will remain under pressure due to higher input prices and fuel & power costs.

Key Risks

- Changes in regulation/policy by the state or central government on alcohol distribution/selling policy would be a key risk to GSL's consumer business.
- Any delay in the operation of new capacities would act as a key risk to GSL's earnings in the near term.

Additional Data

Key management personnel

Vivek Gupta	Chairman
Ajay Kumar Swarup	Managing Director
Bhaskar Roy	COO
Nilanjan Sarkar	CFO
Santosh Kumar Pattanayak	Company Secretary

Source: Company Website

Top 8 shareholders

Sr. No.	Holder Name	Holding (%)
1	Massachusetts Institute of Technology	3.82
2	Old Bridge Capital Mgmt Pvt Ltd	1.95
3	INTL Asset Recons	1.87
4	Samar Voyager LLP	1.8
5	Wisdom Tree Investments Inc	0.06
6	Power Corp of Canada	0.06
7	American Century Cos Inc	0.03
8	State Street Corp	0.03

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

Sharekhan

by BNP PARIBAS

Know more about our products and services

For Private Circulation only

Compliance Officer: Ms. Binkle Oza; Tel: 022-61150000; email id: compliance@sharekhan.com;

For any queries or grievances kindly email igc@sharekhan.com or contact: myaccount@sharekhan.com.

Registered Office: Sharekhan Limited, The Ruby, 18th Floor, 29 Senapati Bapat Marg, Dadar (West), Mumbai – 400 028, Maharashtra, INDIA, Tel: 022 - 67502000/ Fax: 022 - 24327343. Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O/ CD) / MCX - Commodity: INZ000171337; DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669; Research Analyst: INH000006183.