



“Globus Spirits Limited Q3 FY-18 Earnings Conference Call”

**February 19, 2018**



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**Moderator:** Good morning, ladies and gentlemen. Welcome to the Globus Spirits Conference Call. As a reminder, all participant lines 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 the conference call, please signal the operator by pressing ‘\*’ then ‘0’ on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Santosh Patnaik from Globus Spirits. Thank you and over to you, sir.

**Santosh Patnaik:** Good morning and welcome to Q3 & 9 months FY18 earnings conference call of Globus Spirits Limited. We are joined by senior members of the Management Team including Mr. Shekhar Swarup – Joint Managing Director; Mr. Vijay Rekhi – Executive Director; Dr. Bhaskar Roy – Executive Director & COO and Mr. Ajay Goyal – CFO.

We will commence the call with opening remarks from the management team following which we will have an interactive question-and-answer session.

Before we begin I would like to highlight that some statements made in today’s call may be forward-looking in nature and a disclaimer to this effect has been included in the results presentation shared with you earlier.

I would now like to invite Mr. Shekhar Swarup to share his initial remarks.

**Shekhar Swarup:** Thank you. Good morning everyone. I trust all of you would have received and gone through the earnings presentation that was circulated earlier. Let me begin by sharing the key developments while Dr Bhaskar Roy will brief you on operational performance and Mr. Vijay Rekhi will update you on Unibev’s performance in the last quarter. And finally our CFO Mr. Ajay Goyal will talk you through the financial highlights for the quarter ended December 2017.

Our West Bengal facility scaled up well combined with robust performance production volumes and other facilities. We believe that with our highly capable technical and operations team we would be able to further enhance production moving beyond the current utilization levels.

Currently our captive consumption of bulk alcohol is at about 43% which is expected to further increase with growth in IMIL volumes and will further strengthen with our franchise bottling operations. Capacity utilization at the company level stood at 100% for the quarter gone by.

Haryana IMIL continues to be challenging as reported industry volumes declined year-on-year and competition banks heavily on heavy channel incentives to garner market share. We are focusing on brand building to counter these adverse conditions. In the medium term the strategy will pay good dividend as our brands withstand to gain share as growth returns in the market.



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Coming now to profitability. Despite healthy double digit revenue growth of 19% year-on-year absolute EBITDA was similar to Q3 FY17. Profit margins declined due to change in product mix in favor of manufacturing and the situation was worsened due to a decline in IMIL in Haryana.

We expect profitability to improve as consumer business picks up. We are expanding our footprint in West Bengal and focusing on brand building in both Haryana and West Bengal. We are well positioned to create strong shareholder value as we increase contribution from our consumer business and expand our IMFL footprint. Premium IMFL is an integral part of our 360 degree business model and we will be adopting a phased approach in this business both for launch of brands and for geographic expansion.

The strategy is to allocate free cash flow out of Globus' IMIL and distillery operations into IMFL and ramp up as soon as there is proof of concept. I would now like to request Mr. Vijay Rekhi, Chairman Unibev to give an update on Unibev's operations for the quarter gone by.

**Vijay Rekhi:**

Good morning gentlemen. In Q3 FY18 we launched our first premium IMFL product from the stable of Unibev. A premium brandy named Laffaire in the State of Pondicherry to start with and that was in December of 2017. The initial response has been extremely encouraging, the product has been well received both by consumers and channel partners both the blend and the premium packaging have been appreciated.

This has given us lot of motivation and confidence and we are now poised to launch not only this brand the outside of Pondicherry but along with it three premium whiskies at top of the pyramid in terms of pricing to start with in certain states of Andhra Pradesh, Telangana and Karnataka along with Pondicherry.

These will be rolled out from April of 2018. These brands carry strong and differentiated unique selling proposition for the consumers and this differentiation along with the effective packaging we believe will be sort of the approach for the consumer to franchise these products.

All these products as I said are sitting on top of the pyramid as a high profit point and these segments in the premium sort of arm of segment of IMFL are highly profitable though there is a strong competition from established companies, we believe consumer choice is limited in these product categories and therefore as we bring a unique selling proposition it will enable consumers to widen their choice and hopefully we would offer a very, very effective alternative.

Now I request Dr. Bhaskar Roy to share the operational performance of the company.

**Dr. Bhaskar Roy:**

Thank you, Mr. Rekhi. Good morning and warm welcome to everyone. I will share the operational performance of Globus Spirits Limited during the quarter ended December 31, 2017.



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As highlighted earlier this was a mix quarter for us. While we continue to demonstrate healthy revenue growth driven by the manufacturing business our profitability declined due to change in manufacturing mix. During quarter 3 FY18 growth in manufacturing business stood at 26% while consumer revenues grew by 6%.

Contribution of consumer and manufacturing business came in at 40% and 60% respectively. Growth in bulk alcohol revenue stood at 45% with similar growth in volumes driven by increased sales contribution from the West Bengal facility. Franchise IMFL volume stood at 0.87 million cases in Quarter 3 FY18 compared to 1.04 million cases in the corresponding quarter of last year.

IMIL volumes came in at 3.26 million cases during the quarter, higher by 7% against the same period last year led by robust volume growth of 18% in Rajasthan. IMIL market share in Rajasthan stood at 32% in a growing market. In Haryana sales volumes came under pressure declined 30% year-to-year due to adverse market conditions.

While we believe this situation would change over the long run there seems to be no immediate reprieve except focusing on brand building. Moving to other segment, our high potential DDGS reported a growth of 13% in quarter 3. The growth looks tepid in comparison to the bulk alcohol growth due to low realizations on account decline in soya prices.

We believe that the soya prices may continue to remain low for balance part of quarter 4 FY18. Coming to our Bihar distillery. The Honorable Supreme Court vide order dated 19 January 2018 has dismissed the special leave petition filed by excise department challenging the High Court order dated May 3, 2017 instructing Bihar Government to renew license for manufacturing alcohol.

We remain confident of recommending our operations after the license we received which will have positive impact on our overall profitability. With that I would like to call up on our CFO, Mr. Ajay Goyal to continue the discussions on the financial performance.

**Ajay Goyal:**

Thank you, Dr. Roy. Good morning everyone. I will take you through the key financial highlights for the quarter ended December 31, 2017. Our Q3 FY18 gross revenues stood at Rs. 4,544 million higher by 43% year-on-year basis. EBITDA came in at Rs. 177 million similar to last year Q3 EBITDA. Q3 EBITDA margins declined by 130 basis points to 6.8%.

We believe that changing product mix in favor of IMIL will drive margin improvement going forward. Profit after tax during the quarter stood at Rs. 13 million compared to Rs. 40 million in Q3 FY17.

Moving to product line wise performance. In Q3 FY18 we sold 3.2 million cases of IMIL with an average net realization of Rs. 314 per case. In franchisee IMFL business the aggregate volume



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for the quarter was 0.87 million cases out of this 0.32 million cases pertains to bottling done by ABD in Rajasthan; 0.24 million cases for bottling done for USL in Haryana and the remaining 0.31 million cases for bottling done for USL in West Bengal.

Our bulk alcohol volumes stood at 19 million bulk liters compared to 13 million bulk liters in Q3 FY17. The total revenues from manufacturing stood at Rs. 1,559 million in the quarter. While the revenue from customer business stood at Rs. 1,024 million. The total outstanding debt as on December 31, 2017 including the working capital stood at Rs. 2,549 million.

This concludes my remarks on the financial highlights. I would now request the moderator to open the forum for questions. Thank you.

**Moderator:** Thank you. Ladies and gentlemen, we will now begin the question-and-answer session.

We will take the first question from the line of Yash Agarwal from Crest Capital. Please go ahead.

**Yash Agarwal:** Sir, I had a first question on this other expenses. So they have gone up by approximately 31% year-on-year and 14% quarter-on-quarter. I just wanted to understand what has triggered such a rise in the other expense?

**Shekhar Swarup:** This is largely to do with the growth in the franchisee bottling business. I will request Ajay Goyal to explain that further.

**Ajay Goyal:** See, the way Shekhar told, the largest part of the expense variation is coming from the IMFL growth and secondly basically there is an increase in the production in this quarter as compared to previous quarter. That is why there is an increase in the cost for other expenses like fuel. And second point, there is a drastic increase in the cost of fuel. That is why our profitability margins are down.

The price of the raw materials, prices have gone up drastically in this quarter and third is basically little more expensive on repairs and maintenance due to shut in our Samalkha and Bengal units for certain maintenance expenses. These are the largest expenses which has contributed the major increase in these variants.

**Yash Agarwal:** Repair and maintenance would be one time in nature, right?

**Ajay Goyal:** Yes it is one time nature, yes.

**Yash Agarwal:** So what would the amount that you spent in repair and maintenance?



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- Ajay Goyal:** The variance from previous quarter is somewhere around Rs. 60 lakhs.
- Yash Agarwal:** I had another question since the fuel prices have risen are we not offsetting it by passing it on to the consumers?
- Shekhar Swarup:** So yes, we have been able to do that partially. The other factor that propped up fuel prices for us is that in the NCR region where two of our factories are located, Haryana and Rajasthan factories there was a ban on pet coke as a fuel. As a result we had to immediately shift a part of our fuel purchase which was pet coke to rice husk. This also led to higher R&M cost because there was some retrofitting of its shipment that needed to be done. So this was sort of an unexpected situation that happened. But over the course of the next few quarters, we should be able to work on further lowering our share of cost from fuel.
- Yash Agarwal:** How many quarters would that take for it to moderate the other expenses?
- Shekhar Swarup:** On the cost of fuel side, it is difficult to say because that is the commodity cycle. But we are taking certain measures to reduce this and hopefully in the next one or two quarters this will get reduced.
- Yash Agarwal:** When you say the company operated at 100% capacity utilization I mean Haryana is not doing as well and Bihar is not contributing so then what sense are you saying that the company is at 100%?
- Shekhar Swarup:** Well, besides Bihar of course, this is from our plant capacity for the quarter. We were able to achieve that utilization.
- Yash Agarwal:** Also Haryana after decent growth in Q2, it is again been struggling. So what is the idea here and how do we plan to move about to get this factory up and running in a profitable way as it is significantly underutilized right now Haryana? What is your plan there sir?
- Shekhar Swarup:** So as I mentioned earlier, there are certain adverse market conditions which have led to reduction in the market. Because the reduction in the market there is significant over capacity in Haryana. And suppliers, manufacturers are leading to very high channel incentives in order to retain market share. We are focusing on our brand building efforts so that our market shares remain at the levels that they were in Q2 and even earlier and which is what we have seen.
- We have retained 11% to 12% kind of market shares even in Q3. Going forward as the growth returns, which is essentially a regulatory reform that needs to take place, we will be able to get a larger market share at that stage. But for the near term, there is going to be a little bit of sort of patience required in Haryana.



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- Yash Agarwal:** Now what are these regulatory reforms in Haryana that you are talking about?
- Shekhar Swarup:** Essentially organizing the distribution, getting certain they are talking of getting a corporation into place so that will help growth coming in. Pricing is something that they need to look at. So we are hopeful that in the next excise year we will hear some good reforms from the government.
- Yash Agarwal:** Also you have been talking about the price hike in Rajasthan and you know Rajasthan is a very significant market for us, so has that come about or are you expecting it to come about?
- Shekhar Swarup:** We are expecting it to come about but this is the time February-March when all excise policies are being worked on. So we will know very soon for both states.
- Yash Agarwal:** And just from an understanding perspective since it contributes about IMIL about Rs. 80 crores per quarter in Rajasthan, so 5% to 10% hike would directly add to the revenue? Is that understanding, right?
- Shekhar Swarup:** Yes.
- Yash Agarwal:** And the profit margins would be substantial right on that?
- Shekhar Swarup:** Well, if you look at if you compare Q4 to Q1 and if there is a price hike which is before Q1 then all of it goes to the profit as compared to Q4.
- Yash Agarwal:** Okay, so basically you are saying on a quarter-on-quarter basis whatever price hikes there will be will float to the EBITDA?
- Shekhar Swarup:** Yes but we have to see over the course of the year the inflation on cost as well.
- Yash Agarwal:** A question on Bihar supposedly you start I mean you have been saying that it should start by FY19 once you get the license I mean hopefully you get the license. So what sort of revenue contribution can this make over the next two years, the Bihar unit?
- Shekhar Swarup:** So it will make about from our estimates about Rs. 100 crores to Rs. 125 crores of revenue.
- Yash Agarwal:** Okay and that would be at what utilization level, sir?
- Shekhar Swarup:** At 90%.
- Yash Agarwal:** So Rs. 100 crores to Rs. 125 crores so the peak revenue can be about Rs. 150 crores is what you are saying?



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- Shekhar Swarup:** Yes, Rs. 125 crores would be peak I think.
- Yash Agarwal:** Also sir question on IMFL. So how has been so if I heard you correctly you are launching three more whisky brands is it three more whisky or one more?
- Shekhar Swarup:** Three more.
- Yash Agarwal:** Three more, okay. So basically we will have four brands up and running by FY19?
- Shekhar Swarup:** Yes.
- Yash Agarwal:** So what sort of revenues is an internal target from the IMFL side?
- Shekhar Swarup:** So I am sort of stepping on Mr. Rekhi's toes but very quickly I think it is currently we are in proof of concept stage. It is too early to look at revenue and EBITDA projections. I think it is important to understand the business model and the vision here. And for that I request Mr. Rekhi to take you through that.
- Vijay Rekhi:** Yes so as Shekhar has said, we have the proof of concept. So what we are doing is we are launching three whiskeys in the top super premium, premium and semi premium segments. These yield maximum contribution to the industry at those price points and are therefore significant in terms of carving out a share of profit of that particular price point in favor of our brands. Including whiskeys we have also going to be launching premium brandy again in the super premium category which gives a high contribution.
- And we believe that the best way would be for Globus to enter into the top end of the pyramid to get this proportionate shall I say returns on deployed capital because the contributions from these brands are expected and are in reality to be highest for the industry players and that is where we have aimed to be in the market.
- And what we are doing is basically, we are not doing carpet bombing in terms of distribution. We are cherry picking in these states and within those states those outlets which yield maximum distribution with so that we are able to optimize the use of working capital which is planned to be deployed.
- Yash Agarwal:** So right now the target is only the southern markets like AP, Karnataka, Telangana and Pondicherry, right?
- Vijay Rekhi:** That is for the next financial year, yes, and then we are also exploring other markets outside of these four southern states. These four southern states have got very high salience in terms of acceptance of brandy at the price points we talked about and also whiskeys. So we are in a sweet



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spot and the other comforting factor is that we will be selling to the corporations so that the outstanding can be minimized when we supply to the distribution chain.

**Moderator:** Thank you. The next question is from the line of Sai Narayan, an individual investor. Please go ahead.

**Sai Narayan:** So what my question is in terms of the West Bengal market so is it like a fixed price point between the IMIL segments like we see in Haryana and Rajasthan? So that is my first question.

**Shekhar Swarup:** Yes, it is.

**Sai Narayan:** Okay so and during the last analyst meet so were discussing on improving the margins of the business where we were discussing on the three moving parts. One is on the grain prices, second is on the price increases in the IMIL segment and third is on the consolidation of the distribution cost. So with respect to price increases were concerned obviously it place with the State Government. So we have only two things under our control the company's control.

One is on the grain prices, another is on the distribution cost. So as you have seen the company has implemented the changes in the distributor in the Haryana market last year to improve the margins. So likewise with respect to the grain prices?

So what I was asking is with respect to the grain prices is concerned so we see a volatility in the grain prices which has impacted the margins in financial year 2014 and also in Quarter 2 financial year 2017 where we had seen the price increase up to the extent of 20%. So has the company taken note of this critical factor in the raw material cost and what plans does the company have to enforce that this volatility in grain prices does not happen again? Does the company have any plans with respect to grain prices? That is my question, sir?

**Shekhar Swarup:** So there are a few things that we can do to control our margins. One is like you said distribution and other costs. Besides that there are also our recovery and yields that we work on. And finally the selling price of ENA which is not a fixed price and that is why we speak of 360 degree business model having a hedge between fixed price businesses such as country liquor and moving price business such as our bulk business.

So what we have done on to secure our margins is with some of our customers we have secured conversion cost based ENA pricing where our margins are insulated from the movement on grain price, and this is grain price there is a formula which automatically gives price discovery of ENA.



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So we have done that for about 40% to 50% of our bulk sales and balance portion is what we sell therefore in the open market. As a result, this has been quite successful for us in the last two, three quarters. As a result our ENA contribution has more or less been stable.

**Sai Narayan:**

So with respect to grain prices, are we contemplating anything like assuring some long term contracts with the suppliers for a steady and sure supply of grain prices or with respect to because grain prices we have seen actually because our end product whether it is a country liquor or ENA obviously country liquor gives a good margin for us.

So the end product the price point is fixed by the business by the government whereas with respect to volatility in grain prices is concerned sometimes it even goes to the extent of 20% as we have seen in the Quarter 2 financial year 2017. But to mitigate this are we having any plans of entering into a long term contracts or does we have any plans with respect to grain prices in the IMIL?

**Shekhar Swarup:**

We are exploring various options as of now there are no such contracts in place. We feel rather than blocking our suppliers, we have secured our ENA margins by blocking a conversion rate formula with our customers.

**Sai Narayan:**

And with respect to the last analyst meet, we were discussing on the price hikes in the Rajasthan market. So where we were expecting 5% to 10% every two to three years in the Rajasthan market. So what historically have been the price hike in the Haryana market and what price hike we can expect in the West Bengal market from the government?

**Shekhar Swarup:**

As of now we are expecting no price increases or changes in Haryana and West Bengal.

**Sai Narayan:**

No, I was asking about the historical price hikes we have seen in Haryana?

**Shekhar Swarup:**

More or less we have seen that price hikes are between 5% and 10% every two years in every state.

**Sai Narayan:**

So the same you can expect in West Bengal also?

**Shekhar Swarup:**

Yes.

**Moderator:**

Thank you. The next question is from the line of Navneet Bhaiyya, an individual investor. Please go ahead.

**Navneet Bhaiyya:**

I want to check the excise duty component have increased quite significantly of your topline so is there any excise hike or why it was 30% of your gross sales earlier, it is about 45% now?



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- Shekhar Swarup:** Again it is due to the growth in our franchise business where the entire turnover is in our books especially for West Bengal and Rajasthan. This is not really due to any major changes in our core business of country liquor or ENA.
- Navneet Bhaiyya:** So in terms of working capital you do not require incremental working capital to?
- Shekhar Swarup:** No, this is not our working capital, it is not our profit and loss account really.
- Navneet Bhaiyya:** Okay second was what is your outlook in terms of volumes given that you are already operating at 100%?
- Shekhar Swarup:** So the main driver for volumes will come from IMIL and franchise bottling. So here in West Bengal we are seeing good levels of growth, we are currently operating at about 10% to 15% per month kind of growth in West Bengal. In Haryana for a quarter or two I do not see too much growth coming from IMIL so it is going to be mainly West Bengal that is going to be leading growth.
- Navneet Bhaiyya:** Okay so 10% to 15% growth in West Bengal for the entire company would be in about 4%, 5%, right?
- Shekhar Swarup:** Yes, and that is conversion from country liquor to IMIL which is a high value product.
- Navneet Bhaiyya:** So the margins might improve because in terms of top line growth it could be 4% to 5%?
- Shekhar Swarup:** I think it will be more than that going forward.
- Moderator:** Thank you. We will take the next question from the line of Yash Agarwal from Crest Capital. Please go ahead.
- Yash Agarwal:** Sir, I want to know in West Bengal what is our captive consumption for IMIL currently the mix right now?
- Shekhar Swarup:** I think it is about captive consumption including IMFL and country liquor it would be about 20% to 25%. But that includes IMFL and country liquor.
- Yash Agarwal:** Okay and in Haryana that would be?
- Shekhar Swarup:** I think about 30% to 35%.
- Yash Agarwal:** So how confident are you to ramp this up significantly at least in West Bengal in the next 12 to 18 months?



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**Shekhar Swarup:** No, Haryana capacity is much larger than the West Bengal capacity. So it has to be rated as per that.

**Yash Agarwal:** No, so I am saying on West Bengal are you confident that this mix will breach 50% this year the IMIL mix one?

**Shekhar Swarup:** See our target is to get to about 80% captive and we are very confident of strong growth in IMFL in the franchise IMFL business in West Bengal. It is a new relationship with USL over there and they have clarified to us that the West Bengal facility is a strategic facility for them. So we do hope to at least double our Q3 business with them, but that will happen over the course of the next financial year.

As you understand they too also have to mitigate their risks and it is a phased ramp up. In case of IMIL, we are barely at about 2.5%, 3% market share in West Bengal and the top four or five players there combined have about 60% to 70% market share. So in the very least in the first year to two years we should be targeting 25% market share.

**Yash Agarwal:** The last question on the EBITDA margins given that price hike in Rajasthan may come and mix of IMIL will go up in West Bengal. What sort of EBITDA margins are you targeting next year?

**Shekhar Swarup:** Dr. Roy, could you please take that?

**Dr. Bhaskar Roy:** The EBITDA margin is now around 8-9% we are trying to with the IMIL growth which we are anticipating will come in the next year. It will increase by 3% definitely because IMIL will contribute more to the EBITDA margin.

**Yash Agarwal:** You are saying the 200 basis points on a company level right expansion that you are targeting?

**Dr. Bhaskar Roy:** No, I am telling you have asked for the West Bengal facility.

**Yash Agarwal:** Sir, I am talking about the whole company level?

**Dr. Bhaskar Roy:** The whole company is with the strategy which we are having now, that we are converting more from the bulk business with the in house capacity. That means the consumption of increasing the conversion to IMIL. So that will definitely increase the EBITDA level.

**Moderator:** Thank you. The next question is from the line of Sai Narayan, an individual investor. Please go ahead.

**Sai Narayan:** Sir, in terms of West Bengal market is concerned as we know actually West Bengal has organized its own distribution operation. So what is the nature of the business transactions



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because when you are supplying liquor to the distribution corporation, is it on upfront cash 100% cash basis or is it partially credit and partially cash? And if credit is given how many days or how many months the credit is given to the distribution corporation?

**Shekhar Swarup:** It is entirely on credit and it is about seven to ten days credit.

**Sai Narayan:** Okay so in the bottling segment is concerned when we have gone through the last analyst meet, so we were talking about the duty cost actually. The duty cost is borne by the bottler or the brand owners like United Spirits? So I want to know who is bearing the duty cost, is it from the company side Globus Spirits is bearing the duty cost?

**Shekhar Swarup:** I assume you are talking about the country liquor duty in West Bengal?

**Sai Narayan:** No, I am talking about the franchise IMFL business?

**Shekhar Swarup:** That is borne by the brand owner.

**Sai Narayan:** Okay so the capital will not be deployed there right so the brand owners like United Spirits Limited they will be paying for it upfront?

**Shekhar Swarup:** They will be using their own capital to fund duties, yes.

**Sai Narayan:** So this duty cost actually we are discussing I may be ignorant, so what I am asking is has it to be paid in the beginning of the financial year itself to the government?

**Shekhar Swarup:** No, it is paid on every dispatch.

**Sai Narayan:** So as and when it is dispatched out of the factory or something we have to pay?

**Shekhar Swarup:** Correct.

**Moderator:** Thank you. The next question is from the line of Navneet Bhaiyya an individual investor. Please go ahead.

**Navneet Bhaiyya:** Just one more question. The Rajasthan price hikes this has been an election year for Rajasthan. Does that have any impact on the hike coming in this year or historically what have you experienced?

**Shekhar Swarup:** No, I do not think so. I do not think those matters are related per se. We see that as a trend every two years there is a price increase and it has been two years since the last and the next year will be the third year and therefore there will be a price increase.



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**Moderator:** Thank you. As there are no further questions, I now hand the conference over to Mr. Santosh Patnaik for his closing comments.

**Santosh Patnaik:** Thank you everyone for joining us on the call today. Hope we were able to answer all your questions. Should you need any further clarifications or would you like to know more about the company, please feel free to contact us. Thank you.

**Moderator:** Thank you. Ladies and gentlemen, on behalf of Globus Spirits, that concludes today's conference. Thank you for joining us and you may now disconnect your lines.