Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Dixon Technologies Ltd

Healthy Q1; bright prospects

Capital Goods	Sharekhan code: DIXON
Reco/View: Buy ↔	CMP: Rs. 3,700 / Price Target: Rs. 4,500 ↓

↑ Upgrade ↔ Maintain ↓ Downgrade

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		↔	

ESG Disclosure Score NEW

ESG RISK RATING 16.33

Updated July 8, 2022

Low Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

Company details

Market cap:	Rs. 21,960 cr
52-week high/low:	Rs. 6244/3,181
NSE volume: (No of shares)	3.7 lakh
BSE code:	540699
NSE code:	DIXON
Free float: (No of shares)	3.9 cr

Shareholding (%)

Promoters	34.3
FII	15.1
DII	8.1
Others	42.6

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	1.8	-14.3	-14.3	-18.0
Relative to Sensex	-3.2	-12.5	-13.6	-24.2

Sharekhan Research, Bloomberg

Summary

- We retain a Buy on Dixon Technologies (Dixon) with a revised PT of Rs. 4,500 given promising growth outlook backed by robust demand in its key segments.
- Consolidated Q1FY23 sales were in-line with estimates, while the bottom-line missed our estimates. Sales were healthy led by strong growth in lighting products, home appliances and mobile segments. OPM was restricted to 3.5% due to inventory and forex loss.
- Management expects margin to rise and be in the range of 4-4.4% backed by price increases, operating leverage due to higher volumes and backward integration.
- Revenue growth would be aided by new verticals like washing machines (WMs), refrigerators, customer additions and increase in volumes in mobile and WMs.

Dixon Technologies (India) Limited's (DIXON)'s consolidated Q1 sales were in-line with our estimates, while profit missed our expectations. Top-line increased by ~53% y-o-y to Rs 2,855 crore. Operating profit jumped 109% y-o-y to Rs 100cr (in line with estimates) led by strong sales. OPM improved by 94 bps to 3.5% in Q1FY23 as margin increased in all the segments. Adjusted PAT increased by ~152% y-o-y to ~Rs 46 crore (vs our estimate of Rs 51 crore). Segment-wise – Mobile phones (46% to total revenue) revenue grew more than three-fold due to the addition of new customers and ramp up in volumes to Rs 1,305 crore and operating margin improved by 110 bps to 2.5%. Consumer electronics (33% of total revenue) declined by 26% y-o-y to Rs 931crore as there was a demand slowdown in the white goods category in Q1FY23, however operating margin has improved by 30 bps y-o-y to 2.7%. Home appliances and lighting products sales also improved by 262% y-o-y and 50.6% y-o-y respectively. OPM also increased by 180 bps and 270 bps in home appliances and lighting products respectively.

Key positives

- Strong revenue growth in mobile phones (46% of revenue) and home appliances (9% of revenue).
- Overall OPM improved y-o-y despite forex and inventory loss.
- Y-o-Y Margin improvement in all the major business verticals

Key negatives

- Decline in revenues in the consumer electronics segment (down 26% y-o-y) due to demand headwinds in white goods category in Q1FY23.
- Operating margin growth was restricted owing to forex loss of Rs 12crore and inventory write-off due to a decline in commodity prices.

Management Commentary

- In lighting products order book is healthy as the company has received orders from UAE and expects an order from Europe as well. The company is also foraying into smart lighting. Margins are expected to further rise from Q3FY23 onwards.
- In WMs, the order book is strong and the company is delivering 1,50,000-1,60,000 units per month and has marquee clients like Bosch, Lloyd and Croma. In fully automatic, the company is clocking 20,000 units p.m. which is expected to increase further led by customer acquisition and pick-up in demand.
- The company sold 7.4 lakh TV units in Q1FY23 and expects to achieve 1.1 mn sales in Q2FY23.
- Dixon expects contribution from mobile phones to improve due to increasing sales for Motorola, backward integration and addition of one big client.
- More and more global brands are looking for outsourcing solutions and therefore long-term business outlook is robust.

Revision in estimates – We have largely maintained our estimates for FY2023-24E.

Our Call

Valuation – Retain Buy with a revised PT of 4,500: Dixon Technologies is well poised to be one of the key beneficiaries from the government's impetus on increasing domestic manufacturing through PLI schemes. The company has been continuously expanding capacities in its existing verticals and is now backward integrating and expanding into other verticals such as refrigerators, LED monitors, AC components and other hardware products. The company is on a strong growth trajectory over the next 3-4 years with the management targeting to triple its size through customer acquisition across verticals, foray into new products, backward integration and growth in exports. We maintain our Buy rating on the stock with a revised PT of Rs. 4,500.

Key Risks

- Slowdown in consumer discretionary spending and discontinuation of business from key customers might affect revenue growth.
- Adverse raw-material prices, delay in the ability to pass on price hikes adequately, and adverse forex fluctuations might affect margins.

Valuation (Consolidated) Rs cr

Particulars	FY21	FY22	FY23E	FY24E
Revenue	6,448	10,697	15,297	19,814
OPM (%)	4.4	3.5	4.0	4.3
Adjusted PAT	159	190	338	525
% y-o-y growth	32.7	19.3	78.0	55.0
Adjusted EPS (Rs.)	26.9	32.0	57.0	88.4
P/E (x)	137.8	115.5	64.9	41.9
EV/EBITDA (x)	75.5	81.0	35.9	26.6
RoCE (%)	27.4	25.6	32.2	36.7
RoNW (%)	24.9	24.5	31.5	35.1

Source: Company; Sharekhan estimates

Stock Update

Result Update

Good performance across verticals

Dixon Technologies (India) Limited's (DIXON)'s consolidated Q1 sales were in-line with our estimates, while profit missed our expectations. Top-line increased by ~53% y-o-y to Rs 2,855 crore. Operating profit jumped 109% y-o-y to Rs 100crore (in line with estimates) led by strong sales. OPM improved by 94 bps to 3.5% in Q1FY23 as margin increased in all the segments. Adjusted PAT increased by ~152% y-o-y to ~Rs 46 crore (vs our estimate of Rs 51 crore). Segment-wise – Mobile phones (46% to total revenue) revenue grew more than three-fold due to the addition of new customers and ramp up in volumes to Rs 1,305 crore and operating margin improved by 110 bps to 2.5%. Consumer electronics (33% of total revenue) declined by 26% y-o-y to Rs 931 crore as there was a demand slowdown in the white goods category in Q1FY23, however operating margin has improved by 30 bps to 2.7%. Home appliances and lighting products sales also improved by 262% y-o-y and 50.6% y-o-y respectively. OPM also increased by 180 bps and 270 bps in home appliances and lighting products respectively.

New verticals and customer addition would drive growth

The company is confident of strong revenue growth as its expanding capacities in existing verticals of which mobile is a key vertical. It is also foraying into new verticals through various JVs under the PLI scheme. The company is likely to add a leading Japanese brand as its customer in the WM space. In mobile phones, apart from Motorola and Nokia, one more client is expected to be added. The company aims strong revenue growth in FY23 which will be led by the mobile division. Further, the company has a strong order book in all its verticals which would aid revenue growth. The operating margin is expected to be between 4.0-4.4% in FY23.

Dixon Technologies Q1FY2023 conference call highlights

- **Home appliances –** The performance of home appliances is likely to be robust backed by a strong order book and operating leverage due to higher volumes expected on account of new customer additions. The company is currently selling 1,50,00 – 1,60,000 units per month and has a capacity of 200,000 units per month. It has clients like Bosch, Lloyd and Croma in the fully automatic WMs and manufactures 20,000 units per month.

- **Lighting –** The company would pass on the increase in input cost to customers and therefore expects margin to improve after a quarter or two. Dixon is expanding its capacity in lighting and also foraying into smart lighting.

- **Mobile –** Mobile is the largest growing vertical with customers like Motorola, Nokia and Samsung. Further, backward integration for Motorola and new customer acquisition would help company achieve sales of Rs 6,500 crore from mobile vertical in FY23.

- **Update on JV with Rexxam –** The company in a JV with Japan-based Rexxam has set up a facility in Noida for manufacturing of printed circuit boards which is now operational. This has strong revenue potential and the company expects healthy profitability from this JV and expects to sell 0.5mn devices per month.

- **PLI incentive –** The PLI incentive during January to June 2022 is around ~Rs 10 crore. The company is likely to receive Rs 18 crore in telecom and Rs 20 crore in lighting under PLI scheme.

- **Debt and cash status –** The company has a net debt of Rs 130 crore and cash & cash equivalents at Rs 360 crore.

Results (Consolidated) **Rs cr**

Particulars	Q1FY23	Q1FY22	YoY (%)	Q4FY22	QoQ (%)
Revenues	2,855	1,867	52.9	2,952.8	(3.3)
Operating Expenses	2,755	1,819	51.4	2,834.6	(2.8)
Operating profit	100.1	47.9	109.1	118.2	(15.3)
Other Income	0.4	0.4	10.5	1.8	(76.9)
Interest	14.4	9.1	58.1	13.9	3.5
Depreciation	24.1	15.0	60.0	19.1	25.8
PBT	62.1	24.1	157.5	86.9	(28.6)
Tax	16.5	5.9	178.5	23.8	(30.4)
Reported PAT	45.4	18.2	150.2	63.1	(28.0)
Adjusted PAT	45.7	18.2	151.7	63.1	(27.6)
Adj EPS (Rs.)	7.7	3.1	151.7	10.6	(27.4)
			bps		**bps**
OPM	3.5%	2.6%	94	4.0%	(50)
NPM	1.6%	1.0%	63	2.1%	(54)
Tax rate	26.7%	24.6%	201	27.3%	(67)

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector View – Demand outlook encouraging, healthy growth prospects

The Indian electronics and consumer durable industry are ~Rs. 4,00,000 crore and growing rapidly. Manufacturing can be a significant growth driver from a medium to long-term perspective, providing enormous opportunities owing to the shift in manufacturing bases outside China and the government's incentives to enhance manufacturing through the Make in India initiative like the PLI scheme which aims to kick-start the process, with strong industry participation.

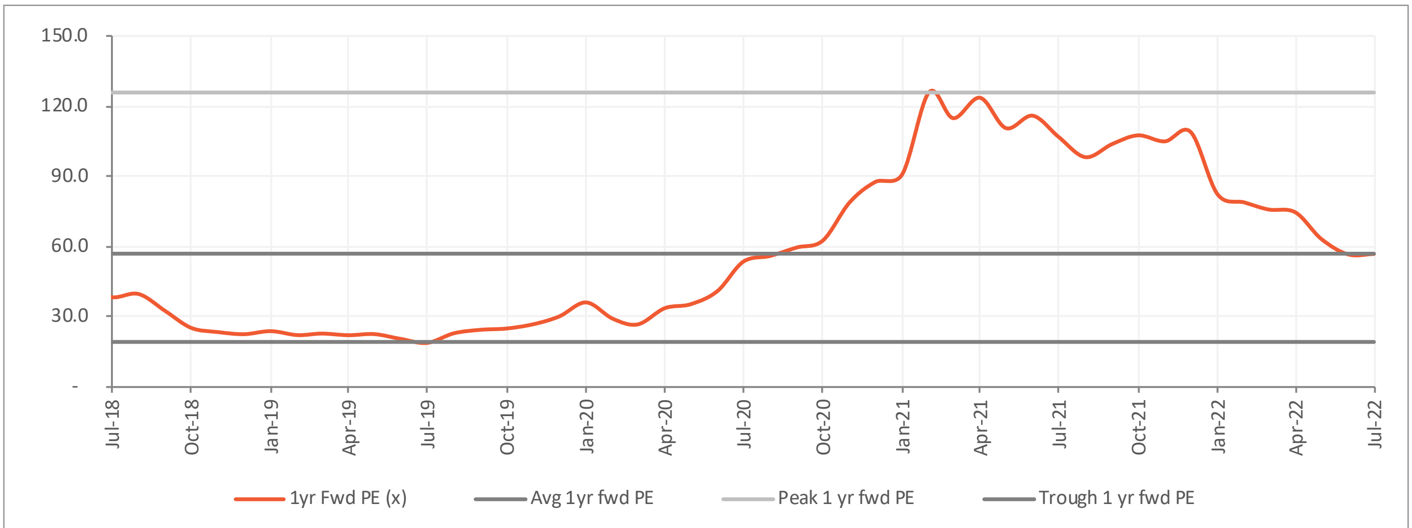
■ Company Outlook – Promising outlook ahead

Dixon's leadership position is a key benefit in the electronic outsourcing business. The company's Tirupati facility is expected to add a new dimension to growth prospects as it will foray into new business verticals, expand the product portfolio of existing business verticals, and penetrate further into South India by forging alliances with original equipment manufacturers (OEMs) and add them as clients. Expanded capacity in consumer electronics and home appliances coupled with a PLI scheme licence for mobile phones is likely to drive revenue growth momentum, while margin may expand due to economies of scale and automation in the lighting business. The company is also applying for PLI schemes in 1) IT (laptops, tablets, hardware) 2) Lighting (extrusions, batons, plastics, mechanicals) 3) AC components and 4) Telecom (modems, routers, IoT devices) which augurs well for long-term growth opportunities.

■ Valuation – Retain Buy with a revised PT of 4,500

Dixon Technologies is well poised to be one of the key beneficiaries from the government's impetus on increasing domestic manufacturing through PLI schemes. The company has been continuously expanding capacities in its existing verticals and is now backward integrating and expanding into other verticals such as refrigerators, LED monitors, AC components and other hardware products. The company is on a strong growth trajectory over the next 3-4 years with the management targeting to triple its size through customer acquisition across verticals, foray into new products, backward integration and growth in exports. We maintain our Buy rating on the stock with a revised PT of Rs. 4,500.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

Founded by Mr. Sunil Vachani, Dixon is a leading manufacturer of products for key consumer durable brands in India. The company currently has 10 state-of-the-art manufacturing units, four in Noida (Uttar Pradesh) and three each in Dehradun (Uttarakhand) and Tirupati (Andhra Pradesh). The company manufactures products with a capacity of 3.4 million LED TVs per year in the consumer durables segment, 20 million LED bulbs per month in the lighting segment, 1.2 million washing machines per year in home appliances, mobile phones, 7 lakh CCTVs, and 1.5 lakh DVDs per month in the security devices segment in India. The company also provides solutions in reverse logistics i.e., repair and refurbishment services of STBs, mobile phones, and LED TV panels. Based on a report, 'Project Rise' by Frost & Sullivan India, Dixon is the largest home-grown, design-focused products and solutions company.

Investment theme

Local manufacturing is expected to get a boost due to increasing emphasis on make in India and government's PLI scheme. The EMS industry is expected to witness a higher CAGR of 30.8% during the same period, as players scale up their offerings from assembly-only to design-led manufacturing. Dixon stands to benefit in the electronic outsourcing business with a leadership position in key business segments. The company's Tirupati facility is expected to add a new dimension to the company's growth prospects, as it will foray into new business verticals, expand product portfolio of existing business verticals, and penetrate further into southern Indian market by forging alliance with OEMs and add them as clients. Moreover, eyes are on the PLI scheme in the mobile phones vertical for which the company has filed few applications.

Key Risks

- A delay in the commissioning of capex projects, slowdown in consumer discretionary spends, and the discontinuation of business from key customers might affect revenue growth.
- Adverse raw-material prices, delay in the ability to pass on price hikes adequately in time, and adverse forex fluctuation might affect margins.

Additional Data

Key management personnel

Sunil Vachani	Executive Chairperson
Atul B. Lall	Executive Director
Saurabh Gupta	Chief Financial Officer
Abhijit Kotnis	Chief Operating Officer
Ashish Kumar	Company Secretary & Compliance Officer

Source: Bloomberg

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Sunil Vachani	26.54
2	Kamla Vachani	7.44
3	Gayatri Vachani	6.64
4	Life Insurance Corporation Of India	5.68
5	Atul B Lall	3.53
6	ICICI Prudential Life Insurance Company Limited	2.05
7	Steadview Capital Mauritius Limited	2.00
8	Nippon Life India Trustee Ltd	1.67
9	Icici Prudential Midcap 150 ETF	1.37
10	Suresh Vaswani	1.10

Source: Capitaline, 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

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