Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Company Update

# Dixon Technologies Ltd

## On a high growth path

| Capital Goods | Sharekhan code: DIXON | | |
|---|---|---|---|
| Reco/View: Buy ↔ | CMP: Rs. 4,263 | Price Target: Rs. 4,960 ↑ | |

↑ 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 Jul 08, 2022

Low Risk

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

*Source: Morningstar*

**Company details**

| | |
|---|---|
| Market cap: | Rs. 25,301 cr |
| 52-week high/low: | Rs. 6,244/3,181 |
| NSE volume: (No of shares) | 3.9 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 | 6.9 | 17.0 | 0.7 | -4.5 |
| Relative to Sensex | 9.6 | 10.7 | 3.3 | 0.6 |

*Sharekhan Research, Bloomberg*


**Summary**

- We retain a Buy on Dixon Technologies (Dixon) with a revised PT of Rs. 4,960 given its leadership in outsourcing consumer electronics/ electronics manufacturing services (EMS) industry, approvals under PLI schemes, a diversified product mix and robust long-term growth outlook.
- Strong manufacturing base across products, capacity expansion/volume growth in washing machines, LED TVs and security systems and new customer additions in mobile, washing machines and IT would drive revenues.
- Ramp-up of high margin original design manufacturer (ODM) products, liquidation of high-cost inventory, cost optimization and a fall in input prices, would improve profitability.
- Healthy balance sheet, low working capital and strong revenue/PAT CAGR of ~33%/~49% over FY22-25E justify its rich valuation.


**Dixon Technologies (India) Limited (DIXON) is a leader in the outsourcing EMS industry with 35% share in LED TV and 50% share in lighting market in India based on capacity. Apart from a strong manufacturing base, the company is building capabilities in designing and aims to capture bigger share of the market through backward integration and capacity expansion. The company boasts of strong clientele in all its product categories, which is being further enriched by addition of marquee global brands to its portfolio. Strong order book across washing machines, mobile, security surveillance system indicates healthy revenue visibility. Operating margin are expected to improve driven by cost optimization, operating leverage, decline in commodity prices and increase in high margin ODM revenues in the long term. Further, Dixon is well poised to be a key beneficiary of several PLI schemes. Recently, it received disbursement of Rs 53 crore under PLI for mobile manufacturing through its subsidiary Padget Electronics. In addition to mobile, Dixon has approval under lighting, IT hardware, air conditioners, wearables and hearables.**

- **Strong manufacturing base and expansion would spur growth:** Dixon has the largest capacity in India in LED television with 6 million sets, which includes backward integration in both LCM and SMT lines. The company services more than 35% of India's total LED TV market. In home appliances, the company has ramped up the capacity of washing machines (washing machines) - semi-automatic category (from 6/14 kgs) to 2.4 million units in Dehradun. The company is India's largest ODM player in lighting, with highest capacity across many SKUs. It plans to invest Rs 100 crore over five years to ramp up the lighting business. Further, in security systems capacity has ramped up from 10 million units per year to 14 million units. We believe existing capacity and further ramp-up in all the verticals should help Dixon in new customer acquisition and drive revenue growth.
- **Strong order book, new products would lead to additional revenue streams:** In lighting, Dixon has received its first export order from UAE and the company expects orders from USA market as well. Dixon is likely to enter into a contract with a large Japanese brand in fully automatic top load (FATL) washing machines for both domestic and global markets. The total capacity of FATL is 600,000 units. In FY23, the company aims to produce ~2,75,000 units. In mobile phones and EMS divisions, Motorola business volumes have a monthly run rate of 400,000 per month. The company has a strong order book of around 1.5 million per quarter from Q2FY23 onwards. The order book for security surveillance system is also healthy. Its JV with Rexxam to manufacture inverter controller board for air conditioners is now operational in Noida. This vertical has strong revenue potential with healthy EBITDA margins and a large export market opportunity. In IT products, the company is likely to tie up with a global brand for commercial production of laptops and it will be a substantial revenue contributor to its business. Dixon has forayed into refrigerators, wherein it is building a capacity of 1.2 million DC refrigerators in the categories of 190-235 litres in Noida.
- **Operating margin to improve going forward:** Dixon aims to increase ODM mix in its portfolio while maintaining its growth in OEM products. The company plans to gradually shift some of its existing and new products in OEM to ODM. This shall lead to better margins as ODM margins are 100-150 bps higher vs OEM. Further, in lighting and home appliances; liquidation of high-cost inventory in the channel, cost optimisation and reduction in input prices, would improve profitability. Thus, backward integration and increasing share of ODM revenue should help the company improve margin to over 4.3% in the next couple of years.

**Revision in estimates –** We have introduced FY25E estimates and tweaked FY2023-24E estimates.

**Our Call**

**Valuation – Retain Buy with a revised PT of Rs. 4,960:** Dixon Technologies with its leadership in outsourcing EMS industry is well poised to be one of the key beneficiaries of 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 set for 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. Further, margins are expected to improve backed by cost optimisation, operating leverage and decline in commodity prices. We envisage revenue/PAT CAGR of ~33%/~49% over FY22-25E. We roll forward our estimates to October FY24E EPS and maintain our Buy rating on the stock with a revised PT of Rs. 4,960.

**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 | FY22 | FY23E | FY24E | FY25E |
|---|---|---|---|---|
| Revenue | 10,697 | 15,768 | 20,389 | 25,408 |
| OPM (%) | 3.5 | 3.8 | 4.1 | 4.3 |
| Adjusted PAT | 190 | 310 | 462 | 628 |
| *% y-o-y growth* | *19.4* | *62.8* | *49.0* | *36.1* |
| Adjusted EPS (Rs.) | 32.1 | 52.2 | 77.8 | 105.8 |
| P/E (x) | 133.0 | 81.7 | 54.8 | 40.3 |
| EV/EBITDA (x) | 67.1 | 43.1 | 30.6 | 23.3 |
| RoCE (%) | 21.8 | 26.3 | 32.0 | 34.5 |
| RoNW (%) | 21.9 | 27.0 | 30.4 | 30.6 |

*Source: Company; Sharekhan estimates*

### Capacity expansion in key verticals would spur revenue growth

Dixon has the largest capacity in India in LED televisions with 6 million sets, which includes the backward integration in both LCM and SMT lines. The company services more than 35% of the India's total LED TV market. In home appliances, the company has ramped up the capacity of washing machines - semi-automatic category (from 6/14 kg) to 2.4 million units in Dehradun. The company is India's largest ODM player in lighting, with highest capacity across many SKUs. The company plans to invest Rs. 100 crore over five years in lighting division. Further, in security systems division capacity has ramped up from 10 million units per year to 14 million units. We believe existing capacity and further ramp-up in all the verticals should help Dixon acquire customers and drive revenue growth.

### Strong growth expected across verticals

Dixon's key segment - consumer electronics revenues are expected to improve as open cell (a key component-contributing 60% of the total product price) prices are bottoming out. In lighting, the company has received its first export order from UAE and the company expects orders from USA market as well. Dixon is likely to enter into a contract with a large Japanese brand in fully-automatic top load (FATL) washing machines for both domestic and global markets. The manufacturing of FATL is in the initial stage and the company is manufacturing 20,000 units per month; while the total capacity is 600,000 units. In FY23, the company is targeting to produce ~2,75,000 units. In mobile phones and EMS divisions, Motorola business volumes have a monthly run rate of 400,000 per month. The company has a strong order book of around 1.5 million per quarter from Q2FY23 onwards. The order book for security surveillance system is also healthy. Its JV with Rexxam to manufacture inverter controller board for air conditioners is now operational in Noida. This vertical has strong revenue potential with healthy EBITDA margins and a large export market opportunity. In IT products, the company has tied up with a global brand for commercial production of laptops and it will be a substantial revenue contributor to its business.

### New products to add to revenue streams

Dixon has forayed into refrigerators, wherein it is building a capacity of 1.2 million DC refrigerators in the categories of 190 to 235 liters in Noida. Further, the company is in the final stages of closing an agreement with a large brand with commitment of 0.6 million refrigerators. The production trial should begin by Q1FY24E and commercial production should roll out by Q4FY24E. In telecom products, Dixon has entered into a joint venture with Bharti Enterprises in which Airtel is its anchor customer. The company also plans to foray into routers, modems, and Gigabyte Passive Optical Network (GPONs) with Airtel's assistance. The company is also likely to finalize a deal for the production of tablets and the motherboard of their notebooks, which may be finalised towards Q2FY23 end. Recently, Dixon signed an agreement with google to sub-license rights relating to Android and Google TV. As per Dixon, the partnership will enable the company in offering a cost effective, and high quality experience to its existing customers and potential new brands which will further strengthen the company's market leadership in the LED TV category. In addition, in lighting segment, Dixon entered into an agreement with Delhi based - Ibahn Illumination (Ibahn), where the latter would transfer its cutting edge technologies of smart lighting solutions to Dixon. We believe new products would help the company scale up its business by adding new revenue streams.

### OPM to improve going forward

We believe, increasing mix of ODM and JDM solutions in the consumer electronics segment would support margin improvement. Dixon aims to increase ODM mix in its portfolio while maintaining its growth in OEM products. The company plans to gradually shift its new products in OEM - laptops, wearables, hearables and consumer-end telecom products to ODM. This shall lead to better margins as ODM margins are higher by ~100-150 bps vs OEM. Further, in lighting and home appliances; liquidation of high-cost inventory in the channel,

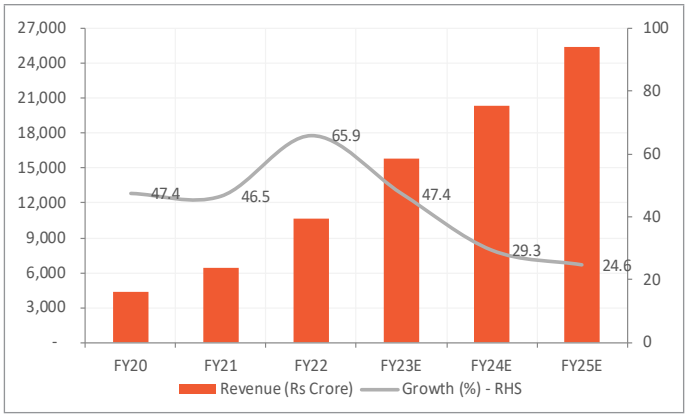
cost optimization and reduction in input prices, would improve profitability. Thus, backward integration in all the business segments and increasing share of ODM revenue should help the company improve margin to over 4.3% in the next couple of years.

**Key beneficiary of PLI and Make in India schemes**

Dixon with its manufacturing capabilities is well poised to be a key beneficiary of several PLI schemes. In mobile, it is the first Indian company to achieve the capex and revenue threshold. Recently, it received disbursement of Rs 53 crore under PLI for mobile manufacturing through its subsidiary Padget Electronics. This scheme extends an incentive of 4-6% on net incremental sale of manufactured goods, including mobile phones and specified electronic components subject to conditions. The total outlay of incentives under the scheme is ~Rs 40,000 crore. In addition to mobile, Dixon has approval under lighting, IT hardware, air conditioners, wearables and hearables. The consumer electronics and IT hardware industry is heavily reliant on imports for sourcing its components. It is expected that PLI scheme and 'Make in India' initiative by the government could help create a robust component ecosystem, which would also reduce current operating cost and encourage local manufacturing.

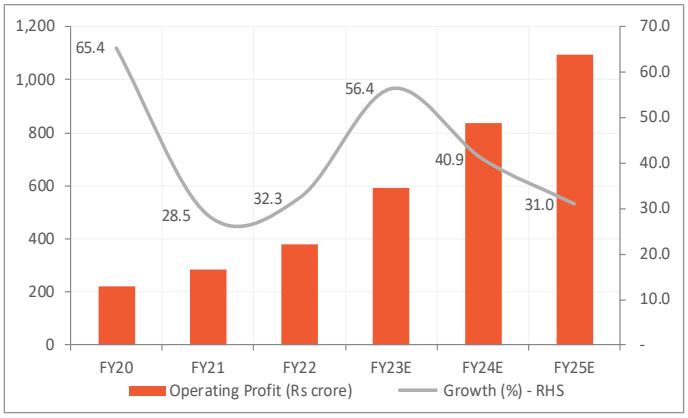
## Financials in charts

### Revenue growth trend



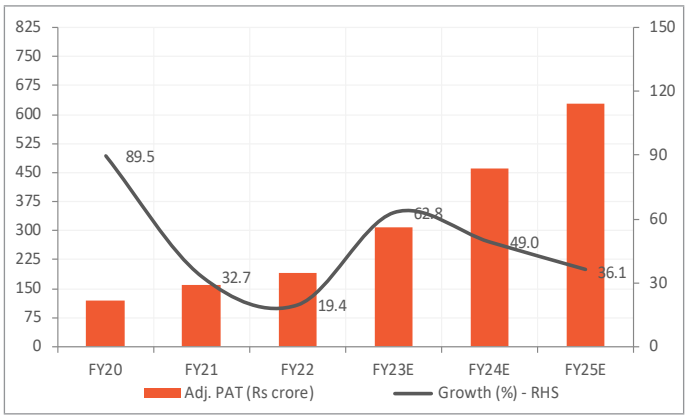

*Source: Company, Sharekhan Research*

### Operating Profit growth trend



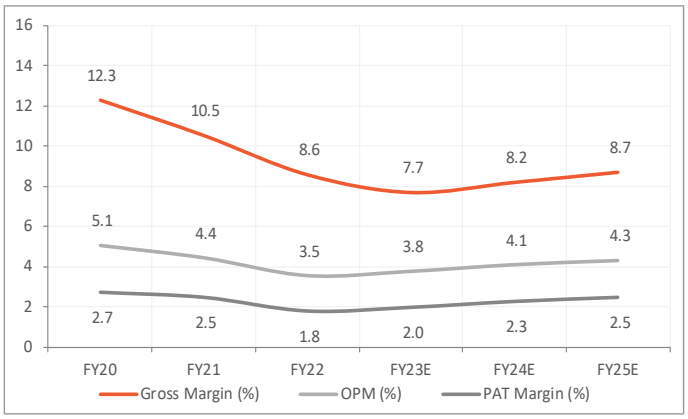

*Source: Company, Sharekhan Research*

### PAT growth trend



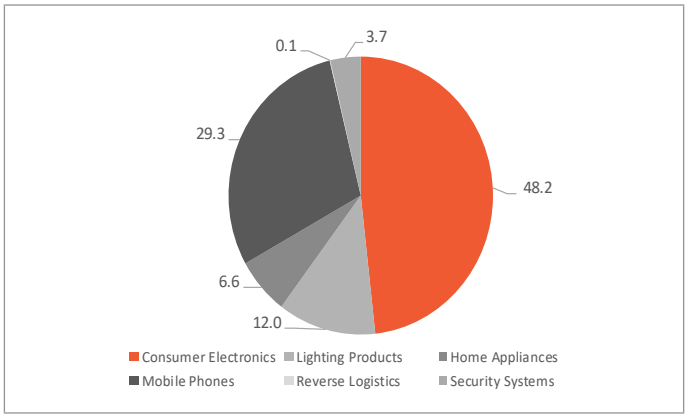

*Source: Company, Sharekhan Research*

### Margin trend



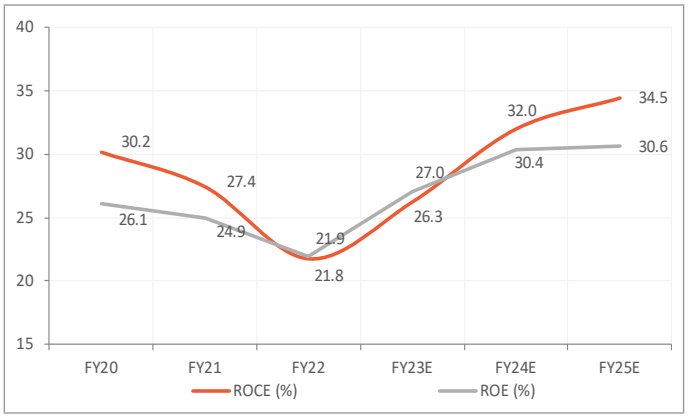

*Source: Company, Sharekhan Research*

### FY22 Segment Revenue Contribution (%)




*Source: Company, Sharekhan Research*

### Return ratios trend




*Source: Company, Sharekhan Research*

## Outlook and Valuation

### ■ Sector View – Demand outlook encouraging, healthy growth prospects

The Indian electronics and consumer durable industry size is ~Rs. 4,00,000 crore and is growing rapidly. The increasing disposable income has given push to the demand for electronics items, particularly smart televisions, smartphones, and laptops. This surge in demand signifies a promising future for the industry. A strong consumer economy and expanding demand for consumer and industrial electronics have propelled the growth of the Indian consumer electronics sector. Manufacturing can be a significant growth driver from a medium to long-term perspective, providing enormous opportunities owing to the shift in manufacturing base outside China and the government's incentives to enhance manufacturing through the Make in India initiative like the PLI scheme which has kick-started the process, with strong industry participation. Further, there is immense localisation potential in the IT hardware sector where USD 5billion worth of equipment is imported annually.

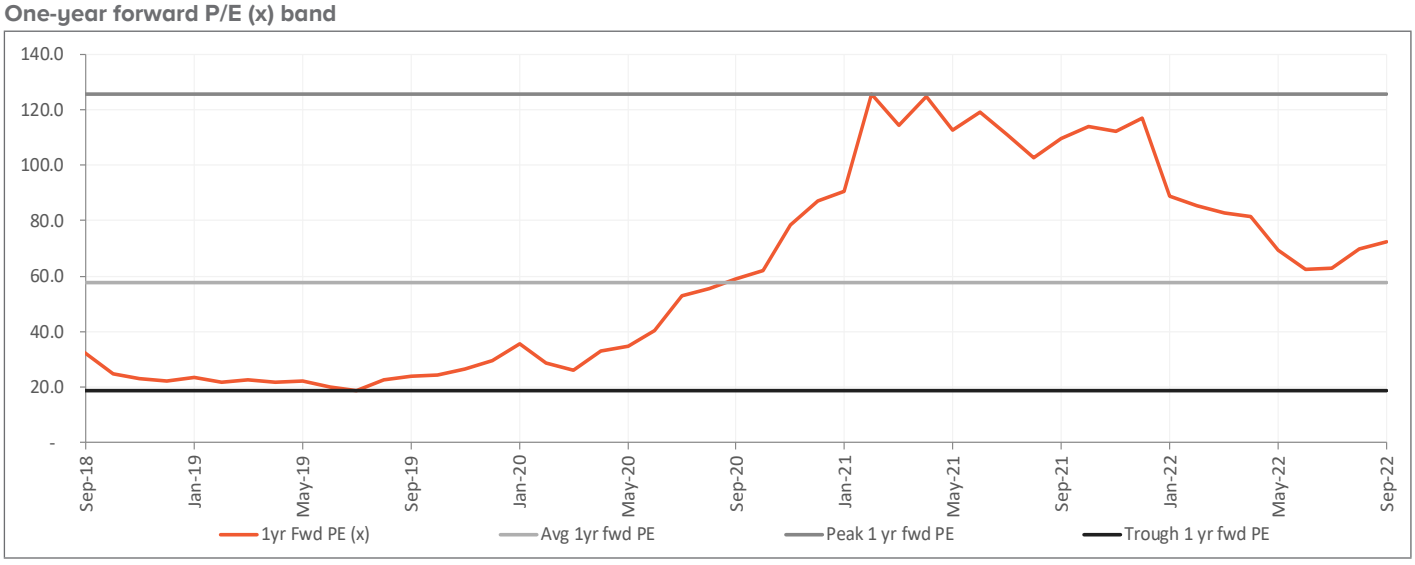
### ■ Company Outlook – Promising outlook ahead

Dixon is a leader 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 and 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 eligible 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 Rs. 4,960

Dixon Technologies with its leadership in outsourcing EMS industry is well poised to be one of the key beneficiaries of 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 set for 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. Further, margins are expected to improve backed by cost optimisation, operating leverage and decline in commodity prices. We envisage revenue/PAT CAGR of ~33%/~49% over FY22-25E. We roll forward our estimates to October FY24E EPS and maintain our Buy rating on the stock with a revised PT of Rs. 4,960.

**One-year forward P/E (x) band**




*Source: Company, 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 6 million LED TVs per year in the consumer durables segment, 20 million LED bulbs per month in the lighting segment, 2.4 million semi-automatic and 0.6 million FATL washing machines per year in home appliances, mobile phones and security devices 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 strong growth 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.

## 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: Company Website*

**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: Bloomberg (Old data)*

## 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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