Stock Update

Result Update

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		↔	

ESG Disclosure Score NEW

ESG RISK RATING 16.33

Updated Oct 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. 25,669 cr
52-week high/low:	Rs. 5,859/3,181
NSE volume: (No of shares)	3.5 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	-0.9	11.0	-0.5	-16.3
Relative to Sensex	-3.9	4.2	-5.1	-14.7

Sharekhan Research, Bloomberg

Dixon Technologies Ltd

Strong volumes but margins stay range-bound

Capital Goods	Sharekhan code: DIXON

Reco/View: Buy	↔	CMP: **Rs. 4,325**	Price Target: **Rs. 4,960**	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

Summary

- We retain a Buy on Dixon Technologies (Dixon) with an unchanged PT of Rs. 4,960 given its leadership in outsourcing consumer electronics/EMS industry, approvals under PLI schemes, a diversified product mix, and robust long-term growth outlook.
- Consolidated Q2FY23 performance was better than estimates with a slight miss on OPM. Sales growth was led by the mobile and home appliances segments. OPM was restricted to 3.8% due to margin drop in mobile segment.
- Management expects ~40% y-o-y growth in revenues and OPM to be @ 3.8-4% in FY23. Long-term margin expansion would be led by backward integration and increasing share of ODM revenues.
- Healthy balance sheet, low working capital and strong revenue/PAT CAGR of ~31%/~47% over FY22-25E justify its rich valuation.

Dixon Technologies (India) Limited's (DIXON)'s consolidated Q2 sales were better than our expectations. The top-line increased by ~38% y-o-y to Rs 3,867 crore. Operating profit jumped 32% y-o-y to Rs 145crore (vs our expectations of Rs 110crore) led by strong sales. OPM, however, declined by 17 bps to 3.8% in Q2FY23 as the margin decreased in the mobile segment. Adjusted PAT increased by ~23% y-o-y to ~Rs 77 crore (vs our estimate of Rs 69 crore). Segment-wise – Mobile phones (41% to total revenue) revenue grew by 166% y-o-y due to the ramp-up of production for existing customers to Rs 1,594 crore, while operating margin declined by 57 bps y-o-y to 2.7%. Consumer electronics (39% of total revenue) remained flattish at Rs 1,500 crore due to a significant decline in open cell prices which led to lower realization for LED TVs, however, operating margin has improved by 43 bps y-o-y to 2.9%. There was a remarkable improvement in home appliance sales at Rs 362 crore (up 62% y-o-y and 42% q-o-q). OPM also increased by 53 bps to 9%. Lighting products sales dropped by 26.6% y-o-y to Rs 290 crore, while the margin improved by 22bps y-o-y to 8.2% in Q2FY23.

Key positives

- Strong revenue growth in mobile phones (~41% of revenue) and home appliances (~9% of revenue).
- OPM improved q-o-q for all the business segments indicating the impact of the decline in raw material cost and ramp-up in volumes on a q-o-q basis.
- Margin in lighting products has improved owing to price hikes and cost optimization measures.
- Long-term OPM guidance @ 3.8-4.5% driven by backward integration and increasing operating leverage.

Key negatives

- Decline in revenues in the lighting products (down 26.6% y-o-y) due to liquidation of inventory.
- Operating margin declined by 17 bps y-o-y due to a dip in OPM in the mobile segment owing to increase in production ramp up cost.
- The company refrained from increasing its revenue and margin guidance for FY23 despite the likely addition of new customers and new products.

Management Commentary

- The recent agreement with Google would help the company address 65% of the Indian LED TV market. Further, many existing brands are also on the Android platform and Dixon is in active discussion with those brands.
- Margin in lighting products has improved as the company has passed on the impact of commodity price hikes coupled with operating leverage and cost optimization measures.
- The company has hired a senior person to help it churn out more ODM solutions in lighting. Capital employed in this business has been reduced by Rs 85 cr due to better asset management.
- The company manufactures features phones for Itel and smartphones and feature phones for Nokia. It is likely to get large orders from a couple of brands from both domestic and export markets and production will begin in Q4FY23.
- The company is confident of more attractive PLI schemes to be launched by the government in IT hardware space.

Revision in estimates – We have marginally tweaked our estimates for FY2023-25E building in the management guidance.

Our Call

Valuation –Retain Buy with an unchanged PT of 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 backward integration, cost optimization and operating leverage. We envisage revenue/PAT CAGR of ~31%/~47% over FY22-25E. We value the stock on September FY24E EPS and maintain our Buy rating on the stock with an unchanged 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	14,942	19,818	24,189
OPM (%)	3.5	3.8	4.2	4.4
Adjusted PAT	190	295	454	609
% y-o-y growth	19.1	55.3	53.8	33.9
Adjusted EPS (Rs.)	32.1	49.8	76.6	102.5
P/E (x)	134.9	86.9	56.5	42.2
EV/EBITDA (x)	68.1	45.4	31.5	24.2
RoCE (%)	21.8	25.2	31.8	33.8
RoNW (%)	21.9	25.9	30.3	30.1

Source: Company; Sharekhan estimates

Mobile and home appliances lead the show

Dixon Technologies (India) Limited's (DIXON)'s consolidated Q2 sales were better than our expectations. Top-line increased by ~38% y-o-y to Rs 3,867 crore. Operating profit jumped 32% y-o-y to Rs 145cr (vs our expectations of Rs 110cr) led by strong sales. OPM, however, declined by 17 bps to 3.8% in Q2FY23 as the margin decreased in mobile segment. Adjusted PAT increased by ~23% y-o-y to ~Rs 77 crore (vs our estimate of Rs 69 crore). Segment-wise – Mobile phones (41% to total revenue) revenue grew by 166% y-o-y due to ramp up of production for existing customers to Rs 1,594 crore, while operating margin declined by 57 bps y-o-y to 2.7%. Consumer electronics (39% of total revenue) remained flattish at Rs 1,500 crore due to significant decline in open cell prices which led to lower realization for LED TVs, however, operating margin has improved by 43 bps y-o-y to 2.9%. There was a remarkable improvement in home appliance sales at Rs 362 crore (up 62% y-o-y and 42% q-o-q). OPM also increased by 53 bps to 9%. Lighting products sales dropped by 26.6% y-o-y to Rs 290 crore, while the margin improved by 22bps y-o-y to 8.2% in Q2FY23.

New customers and additional revenue streams to drive future growth

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. The order book for security surveillance system is also healthy. Its JV with Rexxam to manufacture inverter controller boards for air conditioners is now operational in Noida. This vertical has strong revenue potential with healthy EBITDA margins and a large export market opportunity. Dixon has forayed into refrigerators, wherein it is building a capacity of 1.2 million DC refrigerators in the categories of 190-235 liters in Noida.

Dixon Technologies Q2FY2023 conference call highlights

Consumer electronics: Consumer Electronics volumes have grown by 54% y-o-y. However, the value growth has been flattish at Rs 1,500 crore due to prices of open cells decreasing significantly in the international markets. Margin expansion is due to an increase in ODM/JDM business. The company is in active discussion to offer ODM/JDM solutions to its existing customers. The recent agreement with Google would help the company address 65% of the Indian market. Further, many existing brands are also on Android and Dixon is in active discussion with those brands. The company is setting up an injection moulding plant which should be operational in Q4FY23. In monitors, the company has received an order from DELL for 0.2 mn volumes.

Home appliances – Margins in this category have improved as the company has passed on the impact of commodity price hikes coupled with operating leverage and cost optimization measures. The company has 2.4 mn capacity for 6 kg to 14 kg semi-automatic machines and achieved 1.6 lakh volumes in September month. In fully automatic, the company has 0.6 mn capacity. Bosch is its anchor customer followed by Lloyd and Croma. The company is cloaking volumes of 20-25kper month in this category. The company is in the final stage of getting a contract from a large Japanese brand for its domestic and international markets. The order book is robust and the company is looking to add more customers.

Lighting – Operating margin expanded in line with the company's guidance. Demand is normalizing due to liquidation of inventory and reduction in input price. Dixon is the largest ODM player in lighting and has the largest capacities in LED bulbs. The company would be introducing strips and rope lighting by Q4FY23. The company is working on RFQ for anchor customer in the US market. The company would be making an acquisition for access to blue tooth mesh technology and would be closing the deal in the current quarter with new launches expected in Q1FY24. The company has hired a senior person to help it churn out more ODM solutions. Capital employed in this business has been reduced by Rs 85 crore due to better asset management. The company's first export order in lighting of multiple home solutions will be shipped in current month. The company believes export will be a high point of this business in the next couple of quarters.

Mobile – The company manufactured 1 mn devices for Motorola in Q2FY23. It is planning to deepen the backward integration line. The company manufactures features phones for ITEL and smartphones and feature phones for Nokia. It is likely to get large orders from a couple of brands from both domestic and export markets and production will take off in Q4FY23. It has orders of 3.3 mn units and 2.6 mn units for 2G and 4G respectively for Samsung. The company has hired an R&D head for mobile division.

Security systems – The company is expanding capacity from 10 mn to 14 mn. The company is also backward integrating in this segment through moulding and power supplies.

Telecom – The company has bagged large order from Airtel for set-top boxes for which the production would begin from Q2FY24. The PLI scheme in telecom has been extended by 1 year. The company is in talks with large global brands and aims to launch new products in this business.

Laptop /tablets/IT hardware – Apart from Acer, Dixon would be manufacturing 300k tablets per year for Lenovo. The company is confident of more attractive PLI schemes to be launched by the government in IT hardware space.

Inverter control board for ACs – The company has started manufacturing inverter control boards for ACs in JV with Rexxam. The revenue and profit potential are quite strong in both domestic and export markets. The JV (40:60) would be investing Rs 51 crore over 5 years in this space of which Dixon's share would be Rs 20 crore.

Wearables and hearables – This is the fastest growing market in India. Dixon has a partnership/ JV with Boat and has achieved production of 1 million devices per month. Dixon would also manufacture neckbands and model watches. It is setting up a new plant in Noida which is expected to be operational by December 2022. The company is doing backward integration in this space through SMT lines.

Revenue and margin guidance intact – The company maintained guidance of ~Rs 15,000 crore (+40% y-o-y growth) revenue and OPM @3.8-4% for FY2023. Despite the addition of new products and customers, Dixon has opted for conservative guidance as prices of open cells for LED TVs are still impacting revenue growth. Further, the delay in the ramp of IT hardware and telecom segments and a slowdown in the mobile industry led to delay in order finalization from its anchor customer.

Capex, debt and cash status – Dixon incurred a capex of Rs 185 crore and has guided for capex of Rs 330 crore in FY2023. The capex will be incurred for capacity expansion for PLI scheme and more backward integration in most of the products. The company has a net debt of Rs 140 crore and cash & cash equivalents at Rs 260 crore.

Results (Consolidated) Rs cr

Particulars	Q2FY23	Q2FY22	YoY (%)	Q1FY23	QoQ (%)
Revenue	3,867	2,804	37.9	2,855	35.4
Operating Expenses	3,722	2,694	38.2	2,755	35.1
Operating profit	145	110	32.0	100	45.0
Other Income	1	1	(42.1)	0.4	31.0
Interest	16	9	73.4	14	9.7
Depreciation	29	22	34.8	24	21.0
PBT	101	80	25.6	62	62.4
Tax	23	18	31.2	17	39.5
Reported PAT	77	63	23.1	45	69.8
Adjusted PAT	77	63	23.3	46	69.0
Adj. EPS (Rs.)	13.0	10.6	23.3	7.7	69.0
			bps		bps
OPM (%)	3.8	3.9	(17)	3.5	25
NPM (%)	2.0	2.2	(24)	1.6	40
Tax rate (%)	22.9	21.9	98	26.7	(375)

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.

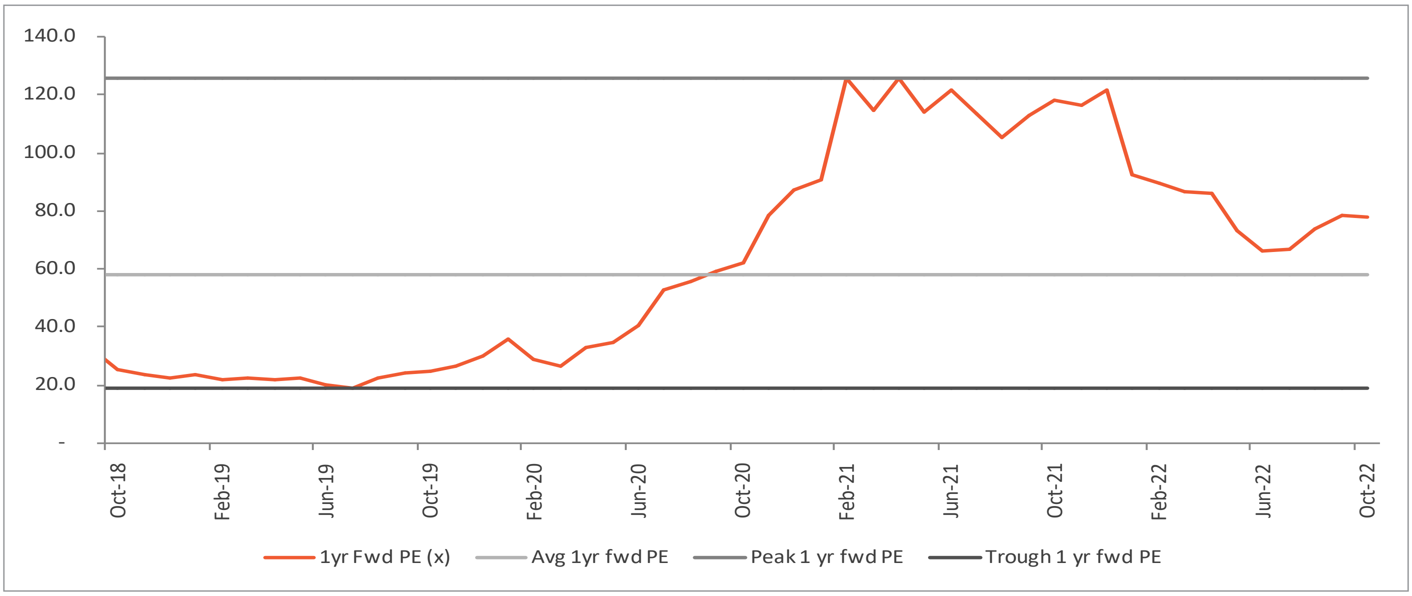
■ Company outlook - Promising outlook ahead

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 license for mobile phones is likely to drive revenue growth momentum, while the 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 an unchanged PT of 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 backward integration, cost optimization and operating leverage. We envisage revenue/PAT CAGR of ~31%/~47% over FY22-25E. We value the stock on September FY24E EPS and maintain our Buy rating on the stock with an unchanged PT of Rs. 4,960.

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 the 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 the product portfolio of existing business verticals, and penetrate further into the South Indian market by forging an 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 a 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 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

Sharekhan

by BNP PARIBAS

Know more about our products and services

For Private Circulation only

Disclaimer: This document has been prepared by Sharekhan Ltd. (SHAREKHAN) and is intended for use only by the person or entity to which it is addressed to. This Document may contain confidential and/or privileged material and is not for any type of circulation and any review, retransmission, or any other use is strictly prohibited. This Document is subject to changes without prior notice. This document does not constitute an offer to sell or solicitation for the purchase or sale of any financial instrument or as an official confirmation of any transaction. Though disseminated to all customers who are due to receive the same, not all customers may receive this report at the same time. SHAREKHAN will not treat recipients as customers by virtue of their receiving this report.

The information contained herein is obtained from publicly available data or other sources believed to be reliable and SHAREKHAN has not independently verified the accuracy and completeness of the said data and hence it should not be relied upon as such. While we would endeavour to update the information herein on reasonable basis, SHAREKHAN, its subsidiaries and associated companies, their directors and employees ("SHAREKHAN and affiliates") are under no obligation to update or keep the information current. Also, there may be regulatory, compliance, or other reasons that may prevent SHAREKHAN and affiliates from doing so. This document is prepared for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. Recipients of this report should also be aware that past performance is not necessarily a guide to future performance and value of investments can go down as well. The user assumes the entire risk of any use made of this information. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors. We do not undertake to advise you as to any change of our views. Affiliates of Sharekhan may have issued other reports that are inconsistent with and reach different conclusions from the information presented in this report.

This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject SHAREKHAN and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.

The analyst certifies that the analyst has not dealt or traded directly or indirectly in securities of the company and that all of the views expressed in this document accurately reflect his or her personal views about the subject company or companies and its or their securities and do not necessarily reflect those of SHAREKHAN. The analyst and SHAREKHAN further certifies that neither he or his relatives or Sharekhan associates has any direct or indirect financial interest nor have actual or beneficial ownership of 1% or more in the securities of the company at the end of the month immediately preceding the date of publication of the research report nor have any material conflict of interest nor has served as officer, director or employee or engaged in market making activity of the company. Further, the analyst has also not been a part of the team which has managed or co-managed the public offerings of the company and no part of the analyst's compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this document. Sharekhan Limited or its associates or analysts have not received any compensation for investment banking, merchant banking, brokerage services or any compensation or other benefits from the subject company or from third party in the past twelve months in connection with the research report.

Either, SHAREKHAN or its affiliates or its directors or employees / representatives / clients or their relatives may have position(s), make market, act as principal or engage in transactions of purchase or sell of securities, from time to time or may be materially interested in any of the securities or related securities referred to in this report and they may have used the information set forth herein before publication. SHAREKHAN may from time to time solicit from, or perform investment banking, or other services for, any company mentioned herein. Without limiting any of the foregoing, in no event shall SHAREKHAN, any of its affiliates or any third party involved in, or related to, computing or compiling the information have any liability for any damages of any kind.

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.

Disclaimer: Client should read the Risk Disclosure Document issued by SEBI & relevant exchanges and the T&C on www.sharekhan.com; Investment in securities market are subject to market risks, read all the related documents carefully before investing.