Sharekhan by BNP PARIBAS

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Stock Update

Result Update

Dixon Technologies Ltd

Muted quarter, cut in revenue guidance; downgrade to Hold

Capital Goods	Sharekhan code: DIXON	
Reco/View: Hold ↓	CMP: Rs. 3,364	Price Target: Rs. 3,770 ↓

↑ Upgrade ↔ Maintain ↓ Downgrade

Summary

- We downgrade Dixon Technologies (Dixon) from Buy to Hold with a revised PT of Rs 3,770 following muted Q3FY23 and a cut in revenue guidance for FY23/FY24.
- Consolidated Q3FY23 performance was below estimates as sales declined by 22% y-o-y. However, the margin improved y-o-y in all the segments. Net profit grew moderately by 12% y-o-y to Rs 52 crore.
- Management scaled down revenue target for FY23 due to slower growth in mobile division and low realization in TV segment.
- We see limited room for an upside from current price levels given expensive valuation post revenue and earnings downgrade. Although long-term prospects are bright, we await better entry point for investors.

Dixon Technologies (India) Limited's (DIXON)'s consolidated Q3 results were below estimates, only outlier being OPM which improved by 127 bps y-o-y to 4.6% (vs our estimate of 3.9%). The top-line decreased by ~22% y-o-y to Rs 2,405 crore. Operating profit grew by 7.9% y-o-y to Rs 111 crore (vs our expectations of Rs 133 crore). OPM improved by 127 bps to 4.6% in Q3FY23 as the margin improved in consumer electronics, mobile, lighting products and home appliances. Adjusted PAT increased by ~12% y-o-y to ~Rs 52 crore (vs our estimate of Rs 69 crore). Segment-wise – Mobile phones (38% to total revenue) revenue declined by 2.6% y-o-y due to low volumes from key customers. Consumer electronics (36% of total revenue) plunged 39% y-o-y to Rs 864 crore due to lower volumes and significant decline in open cell prices which led to lower realization for LED TVs. Home appliance sales increased by 35.5% y-o-y to Rs 244 crore on ramp up in volumes of fully automatic washing machines. OPM in all the key segments improved due to increased share of ODM revenue and value engineering.

Key positives

- Strong revenue growth in home appliances (~10% of revenue)
- OPM improved y-o-y for all the key business segments
- Volumes have been healthy in lighting segment.
- Margin in lighting products has improved owing to price hikes and cost optimization measures.
- OPM guidance of ~ 4% for FY23 driven by backward integration and increasing operating leverage.

Key negatives

- The company cut its revenue guidance for FY23 from Rs 15,000 crore to Rs 12,200-12,500 crore.
- The company reduced mobile revenue guidance for FY23 to Rs 3,800 crore – 4,000 crore from earlier guidance of Rs 4,500-5,000 crore.
- Dixon alluded to the fact that its revenue guidance and growth projections depend on a budget of key customers and any deviation on that front could impact its performance.
- Open cell prices for TV sets declined to Rs 11,500 per unit vs Rs 16,000 per unit in the corresponding quarter of previous year.

Management Commentary

- Consumer Electronics sales were impacted due to lean season after strong pre-Diwali demand in Q2FY23. The company registered TV volumes of 6.9 lakh against 8.3 lakh in Q3FY22, while for 9MFY23, TV volumes grew by 16% y-o-y.
- In home appliances, in the fully automatic washing machine category, the company hopes to double its volumes in FY24. The company is in the final stage of getting a contract from a large Japanese brand for its domestic and international markets.
- Lighting demand was muted in Q3FY23. However, value engineering has led to margin expansion to 9.1% (up 259 bps). It is witnessing a sharp recovery in the institutional business.
- The share of ODM was 24% in 9MFY23 and ~48% of its profits are coming from ODM business.
- In Mobile – volumes from its key customer – Motorola, were muted. The company expects mobile revenue of Rs 3,800- 4,000 crore in FY23, which should double to Rs 8,000 crore in FY24 on addition of new customers.
- The company expects Rs 3,500 crore of revenue in Q4FY23 leading to Rs 12,200-12,700 crore revenue in FY23 and expects OPM of ~4%. The company expects Rs 19,000-21,000 crore revenue in FY24 driven by new customer additions, and higher volume in home appliances and mobile divisions.

Revision in estimates – We have revised our estimates for FY2023-25E following weak results and a cut in revenue guidance, leading to lower earnings estimates.

Our Call

Valuation –Downgrade to Hold with a revised PT of 3,770: Dixon Technologies has reported a weak set of numbers for Q3FY23 and has given muted revenue guidance for its consolidated business largely led by sluggish growth expectations in the mobile division in the near term. We believe cut in revenue guidance would also lead to earnings volatility and therefore we see limited upside from current price levels given rich valuation. Although in the long-term Dixon could benefit from scaling up of its existing verticals, new customer additions and expansion into other verticals such as refrigerators, LED monitors, AC components, and other hardware products. However, we await better entry point for the investors given downgrade in earning estimates and expensive. We value the stock on September FY24E EPS and downgrade the stock from Buy to Hold with a revised PT of Rs. 3,770.

Key Risks

- Slowdown in the consumer discretionary spending and discontinuation or delay in finalization 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	12,214	16,901	20,061
OPM (%)	3.5	3.9	4.3	4.5
Adjusted PAT	190	237	385	502
% y-o-y growth	19.4	24.5	62.7	30.3
Adjusted EPS (Rs.)	32.1	39.9	64.9	84.6
P/E (x)	104.9	84.3	51.8	39.8
EV/EBITDA (x)	53.0	41.9	28.2	22.2
RoCE (%)	21.8	20.7	28.6	30.4
RoNW (%)	21.9	21.4	27.4	27.3

Source: Company; Sharekhan estimates

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 Dec 08, 2022

Low Risk

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

Source: Morningstar

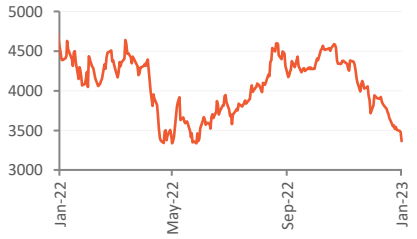
Company details

Market cap:	Rs. 19,965 cr
52-week high/low:	Rs. 4,997/3,181
NSE volume: (No of shares)	2.3 lakh
BSE code:	540699
NSE code:	DIXON
Free float: (No of shares)	3.9 cr

Shareholding (%)

Promoters	34.1
FII	16.7
DII	18.9
Others	30.4

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-6.4	-18.7	-9.8	-24.8
Relative to Sensex	-8.3	-20.6	-18.5	-30.9

Sharekhan Research, Bloomberg

Disappointing quarter

Dixon Technologies (India) Limited's (DIXON)'s consolidated Q3 results were below estimates, only outlier being OPM which improved by 127 bps y-o-y to 4.6% (vs our estimate of 3.9%). The top-line decreased by ~22% y-o-y to Rs 2,405 crore. Operating profit grew by 7.9% y-o-y to Rs 111 crore (vs our expectations of Rs 133 crore) led by decline in raw material cost. OPM improved by 127 bps y-o-y to 4.6% in Q3FY23 as the margin improved in consumer electronics, mobile, lighting products and home appliances. Adjusted PAT increased by ~12% y-o-y to ~Rs 52 crore (vs our estimate of Rs 69 crore). Segment-wise – Mobile phones (38% to total revenue) revenue declined by 2.6% y-o-y due to low volumes from key customers. Consumer electronics (36% of total revenue) plunged 39% y-o-y to Rs 864 crore due to significant decline in open cell prices which led to lower realization for LED TVs. Home appliance sales increased by 35.5% y-o-y to Rs 244 crore on ramp up in volumes of fully automatic washing machines. OPM in all the key segments improved due to increase in share of ODM revenue and value engineering.

Dixon Technologies Q3FY2023 conference call highlights

- **Consumer electronics:** Consumer Electronics sales were impacted due to lean season post pre-Diwali demand in Q2FY23. The company registered TV volumes of 6.9 lakh against 8.3 lakh in Q3FY22 , while for 9MFY23, TV volumes grew by 16% y-o-y. Further, realizations were impacted as open cell prices declined from Rs 16,000 per unit in Q3FY22 to Rs 11,500 per unit. The company expects 3.5-3.6 mn volumes in FY23 (18-20% y-o-y) and therefore expects significant ramp up in the 4th quarter. For FY24, the company expects 15% volume growth. Further, the company is targeting additional 1.5 mn sets in 1.5 years given its google and android platform. Margin profile is also expanding in this division.
- **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. In fully automatic washing machines, the company hopes to double its volumes in FY24. The company is in the final stage of getting a contract from a large Japanese brand for its domestic and international markets.
- **Lighting –** The demand was muted in Q3FY23; however, value engineering has led to margin expansion to 9.1%. However, it is witnessing sharp recovery in the institutional business. The company is expanding its product portfolio and adding new large customers and expects to make decent margin in FY24 as well. Lighting volumes are expected to grow by 15-20% in FY24.
- **Share of ODM:** The share of ODM in total revenue was 24% in 9MFY23 and ~48% of its profits are coming from ODM business.
- **Mobile – Volume from its key customer -** Motorola was muted. The company is close to acquiring a new large customer in a week's time, while another would be added by March end. The company expects revenue of Rs 3,800- 4,000 crore in FY23 which should double to Rs 8,000 crore in FY24.
- **Cut in revenue guidance for FY23/FY24:** The company expects Rs 3,500 crore of revenue in Q4FY23 leading to Rs 12,200-12,700 crore revenue in FY23 and expects OPM of ~4%. The company expects Rs 19,000-21,000 crore revenue in FY24 driven by new customer additions, higher volume in home appliances and mobile divisions.
- **Telecom –** The company has bagged large order from Airtel for set-top boxes for which the production would begin from Q2FY24. The company is in talks with large global brands and aims to launch new products in this business.
- **Laptop /tablets/IT hardware –** In IT hardware, government has introduced a larger scheme which should benefit Dixon. In this segment, its key customers are Samsung and Acer.
- **Capex, debt and cash status:** The company has guided for capex of Rs 330 -360 crore in FY23. The company has a net debt of Rs 68 crore and cash & cash equivalents of Rs 166 crore. During 9MFY23, the company generated free cash flow of Rs 114 crore.

Results (Consolidated) Rs cr

Particulars	Q3FY23	Q3FY22	YoY (%)	Q2FY23	QoQ (%)
Revenue	**2,405**	**3,073**	**(21.8)**	**3,867**	**(37.8)**
Operating Expenses	2,294	2,970	(22.8)	3,722	(38.4)
Operating profit	**111**	**103**	**7.9**	**145**	**(23.4)**
Other Income	3	1	320.9	0.6	412.7
Interest	15	12	26.5	16	(4.2)
Depreciation	29	28	2.9	29	(0.3)
PBT	70	63	9.9	101	(30.8)
Tax	19	17	8.6	23	(19.5)
Reported PAT	52	46	11.9	77	(32.7)
Adjusted PAT	**52**	**46**	**11.9**	**77**	**(32.8)**
Adj. EPS (Rs.)	8.7	7.8	11.9	13.0	(32.8)
Margin			**bps**		**bps**
OPM (%)	4.6	3.4	*127*	3.8	*87*
NPM (%)	2.2	1.5	*65*	2.0	*16*
Tax rate (%)	26.0	26.9	*(95)*	22.9	*310*

Source: Company, Sharekhan Research

Segment-wise revenue and operating profit break-up Rs cr

Revenue	Q3FY23	Q3FY22	YoY (%)	Q2FY23	QoQ (%)
Consumer Electronics	864	1,410	(39)	1,501	(42)
Lighting Products	263	430	(39)	290	(9)
Home Appliances	244	180	35	363	(33)
Mobile Phones	915	940	(3)	1,594	(43)
Security Systems	118	113	5	118	0
Total	2,404	3,073	(22)	3,867	(38)
Operating Profit					
Consumer Electronics	26	30	(14)	43	(39)
Lighting Products	24	28	(15)	24	0
Home Appliances	25	12	106	33	(24)
Mobile Phones	33	28	18	42	(22)
Security Systems	2	5	(58)	4	(44)
Total Operating Profit	110	103	7	145	(24)
OPM (%)			**BPS**		**BPS**
Consumer Electronics	3.01	2.15	86	2.85	(16)
Lighting Products	9.09	6.50	259	8.20	(89)
Home Appliances	10.25	6.73	351	9.01	(124)
Mobile Phones	3.61	2.96	64	2.65	(95)
Security Systems	1.69	4.19	(250)	3.04	135

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector View – Promising long-term demand outlook

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.

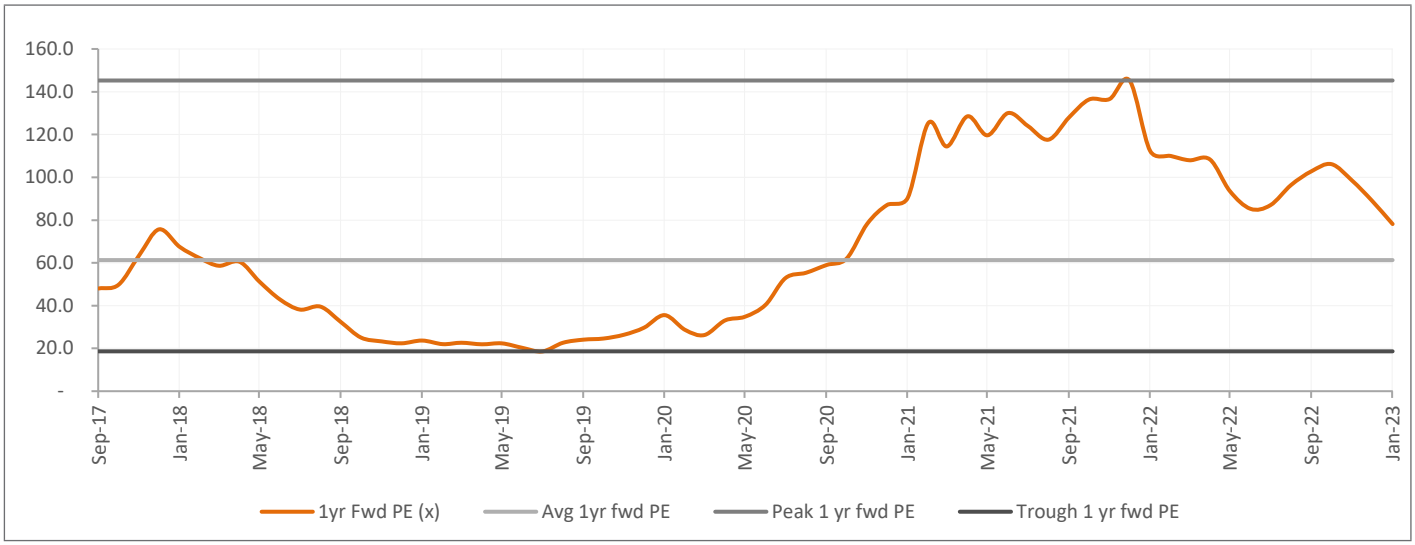
■ Company Outlook – Healthy long-term outlook but near-term weakness to persist

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. However, cut in its revenue guidance and delay in scalability of its mobile business are key concerns which could weigh on its performance.

■ Valuation – Downgrade to Hold with a revised PT of 3,770

Dixon Technologies has reported a weak set of numbers for Q3FY23 and has given muted revenue guidance for its consolidated business, largely led by sluggish growth expectations in the mobile division. We believe cut in revenue guidance would also lead to earnings volatility and therefore, we see limited upside from current price levels given the rich valuation. Although in the long-term Dixon could benefit from scaling up of its existing verticals, new customer additions and expansion into other verticals such as refrigerators, LED monitors, AC components, and other hardware products. However, we await a better entry point for the investors, given the downgrade in earning estimates. We value the stock on September FY24E EPS and downgrade the stock from Buy to Hold with a revised PT of Rs. 3,770.

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 boost due to the 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 benefits in the electronic outsourcing business with a leadership position in key business segments. The company is foraying into new business verticals and expanding its product portfolio of existing business verticals. Moreover, its eying export markets for its products augurs well for long-term growth. An increase in share of ODM revenues would also lead to margin expansion, thereby setting a healthy growth trajectory for the long term.

Key Risks

- A delay in the commissioning of capex projects, the slowdown in consumer discretionary spending, and the discontinuation of business from key customers might affect revenue growth.
- Adverse raw-material prices, delay in passing 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	Life Insurance Corporation Of India	5.72
2	LICI ASM NON PAR	5.00
3	ICICI Prudential Life Insurance Company Limited	2.48
4	Vanguard Group Inc.	2.20
5	Nippon Life India Asset Management	1.73
6	Steadview Capital Mauritius Ltd	1.09
7	Morgan Stanley	1.08
8	Emirate of Abu Dhabi, UAE	1.01
9	DSP Investment Managers Pvt Ltd	1.01
10	Blackrock Inc.	0.90

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

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

Source: Sharekhan Research

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