Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Dixon Technologies Ltd

Strong quarter, valuation limits upside

Capital Goods	Sharekhan code: DIXON

Reco/View: Hold	↔	CMP: **Rs. 3,717**	Price Target: **Rs. 4,050**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

Summary

- Consolidated Q4FY23 performance was strong as operating profit/net profit grew by 32%/28% y-o-y, respectively, led by strong margin improvement in all its key segments.
- Management expects Rs. 6,000 crore revenue (lower than earlier guidance) from the mobile division as two key customers will be added in FY24. Healthy volume growth in TV/washing machines and new product launches in lighting shall aid revenue growth.
- OPM are likely to expand by 20-25bps owing to operating leverage, backward integration and increase in revenue contribution through ODM solutions in consumer electronics and lighting segments.
- We have built in revenue/earnings CAGR of 27%/39% over FY23-FY25E. Currently, the stock trades at ~66x/~45x FY24/FY25E EPS. We believe ramp up in its mobile division holds the key to growth. We maintain Hold on Dixon with a revised PT of Rs 4,050 as we believe current valuations offer limited upside and investors should await a better entry point.

Dixon's Q4 performance was good as despite a marginal miss on sales. There has been a strong beat on margin and profit estimates. Revenues for Q4FY23 on a consolidated basis was up by ~4% y-o-y to Rs 3,065 crore against Rs 2,953 crore in Q4FY22 (vs our estimate of Rs. 3,087 crore). The operating profit for the year was Rs 156 crore against Rs 118 crore in Q4FY22, recording growth of 32% (vs our estimate of Rs. 136 crore). OPM came in at 5.1% as compared to 4% in FY22, and our expectation of 4.4%. The Consolidated PAT for the quarter was Rs 81crore against Rs 63 crore in the same period last year, a growth of ~28% (vs our estimate of Rs. 70 crore). The company has not provided any revenue guidance for FY24 but aims to grow better than the industry. The mobile segment is expected to see revenues around ~Rs. 6,000 crore for FY24.

Key positives

- Strong revenue growth of ~20% in home appliances (~9% of total revenue).
- Mobile segment revenue grew by 9% y-o-y.
- OPM improved y-o-y for all the key business segments except security systems.
- The company indicated that OPM could be between 4.2-4.5% in FY24.

Key negatives

- The company refrained from giving any revenue guidance.
- Open cell prices for TV sets declined to Rs 11,500 per unit vs Rs 16,400 per unit in the corresponding quarter of the previous year. This led to a 3% y-o-y decline in consumer electronics.
- Lighting products revenue declined 11% y-o-y during the quarter.
- Margins in the security systems declined 56 bps y-o-y.

Management Commentary

- Dixon refrained from providing revenue guidance for FY24 but is confident of robust growth across the segments.
- The company aims for further margin expansion of 20-25bps owing to a operating leverage, backward integration and an increase in revenue contribution through ODM solutions in consumer electronics and lighting segments.
- The company may incur a capex of ~Rs.400 crore,, mainly in the mobile segment. For FY23, capex was Rs. 450 crore.
- The company expects Rs. 6,000 crore of revenues in its mobile segment in FY24 as it is in the final stage of signing two key customers. During FY23, Nokia volumes were significant, and the company expects further orders from reliance on 4G phones which would aid growth.
- In consumer electronics TV volumes grew by 15% y-o-y to 3.4 mn units in FY23. However, a correction in open cell prices led to lower realisations.
- The company is expanding its product portfolio in lighting and adding new large customers and expects healthy growth with product addition in new categories in this segment.
- The company received Rs. 9 crore/Rs. 2-3 crore in mobile/telecom under the PLI scheme and would be eligible for PLI in IT hardware and lighting components in FY24.

Revision in estimates – We have revised our estimates for FY2024-25E, factoring in revised guidance for the mobile division and OPM.

Our Call

Valuation – Maintain Hold with a revised PT of 4,050: Dixon Technologies has reported strong Q4 numbers and provided an optimistic outlook for FY24 without any specific revenue guidance. It has toned down its mobile revenue guidance to Rs. 6,000 crore in FY24 but expects to surpass it. We believe, 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. We expect sales/PAT CAGR of ~27%/39% over FY23-FY25E and margin expansion of ~25-30 bps to 4.5% over the same period. However, we await a better entry point for the investors given the expensive valuation as the stock trades at ~66xFY24E EPS and ~45xFY25E EPS. We also reckon that scalability in the mobile division holds the key to growth in the future. We value the stock on FY25E EPS and maintain Hold with a revised PT of Rs. 4,050.

Key Risks

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

Valuation (Consolidated) Rs cr

Particulars	FY22	FY23	FY24E	FY25E
Revenue	10,697	12,192	15,088	19,785
OPM (%)	3.5	4.2	4.4	4.5
Adjusted PAT	190	254	338	495
% y-o-y growth	19.4	33.6	32.8	46.6
Adjusted EPS (Rs.)	32.1	42.7	56.7	83.1
P/E (x)	115.9	87.1	65.6	44.7
EV/EBITDA (x)	58.6	43.0	33.5	25.0
RoCE (%)	21.8	23.2	27.2	32.1
RoNW (%)	21.9	22.3	23.3	26.7

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 May 08, 2023

Low Risk

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

Source: Morningstar

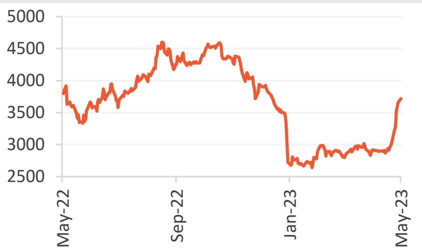
Company details

Market cap:	Rs. 22,135 cr
52-week high/low:	Rs. 4,670/2,553
NSE volume: (No of shares)	3.8 lakh
BSE code:	540699
NSE code:	DIXON
Free float: (No of shares)	3.9 cr

Shareholding (%)

Promoters	34.1
FII	12.1
DII	23.8
Others	30.1

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	27.5	28.5	-13.2	8.6
Relative to Sensex	24.7	21.9	-13.4	-5.9

Sharekhan Research, Bloomberg

Stock Update

Result Update

Strong profitability leads the show

Dixon's Q4 performance was good. Despite a marginal miss on sales, there has been a strong beat on margin and profit estimates. Revenues for Q4FY23 on consolidated basis was up by ~4% y-o-y to Rs 3,065 crore against Rs 2,953 crore in Q4FY22 (vs our estimate of Rs. 3,087crore). The operating profit for the year was Rs 156 crore against Rs 118 crore in Q4FY22 recording growth of 32% (vs our estimate of Rs. 136 crore). OPM came in at 5.1% as compared to 4% in FY22 and our expectation of 4.4%. Consolidated PAT for the quarter was Rs 81crore against Rs 63 crore in the same period last year; a growth of ~28% (vs our estimate of Rs. 70 crore). The company has not provided any revenue guidance for FY24 but it aims to grow better than the industry. The mobile segment is expected to see revenues around ~Rs. 6,000 crore for FY24.

Dixon Technologies Q4FY2023 conference call highlights

Optimistic outlook on growth front: The company did not provide revenue guidance for FY24 but is confident of robust growth across the segments.

Margin guidance: The company aims for further margin expansion of 20-25bps in FY24 owing to operating leverage, backward integration and an increase in revenue contribution through ODM solutions in consumer electronics and lighting segments.

Capex Guidance: The company would incur a capex of ~Rs.400 crore directed mainly in the mobile segment. For FY23, the capex was Rs. 450 crore.

Consumer Electronics: The T.V segment had 15% volume growth in FY23 where in it sold 3.4mn TV units. Further, a correction in the open cell prices led to lower realizations. Apart from its agreement with Google which would help in catering to 65% of the Indian smart TV market, other existing brands are also on Android platform and Dixon is in talks with them for future business partnerships. The company is targeting an additional 1.5 mn sets in 1.5 years given its Google and Android platforms. A backward integration in injection moulding in TV manufacturing would also help in improving margins in this segment.

Mobile: The company expects ~Rs. 6,000 crore of revenues in mobile segment in FY24 as it is in its final stage of signing two key customers. During FY23, Nokia volumes were significant and the company expects further orders from reliance for 4G phones which would aid growth. The margins are expected to improve in FY24 from current levels of ~3.2% owing to higher volumes. The company expects manufacturing in India to increase as many Chinese mobile manufacturers plan to outsource mobile manufacturing.

Lighting: The company is expanding its product portfolio and adding new large customers and expects healthy growth with product addition in new categories in this segment. After getting export orders from new customers in UAE in Q3 and Q4, the company has received its first export order from Germany, which will be included in Q2FY24. The company is also in advanced stages of discussion with potential customers in the US and UK. New modulating products based on blue tooth mesh technology that it acquired from Ibahn Illuminations will be launched in Q2FY24.

Capacity expansion in refrigerators: In refrigerators, Dixon is creating a facility in Greater Noida with a capacity of 1.2 million direct cool refrigerators. This is in the capacity range of 190 litres and 235 liters with multiple features.

Laptop /tablets/IT hardware: In IT hardware, the government has introduced a larger scheme which should benefit Dixon. In this segment, its key customers are Samsung and Acer, which provide healthy order books to Dixon.

Telecom: The company has bagged large orders from Airtel for set-top boxes. The company is in talks with large global brands and aims to launch new products in this business.

Results (Consolidated) Rs cr

Particulars	Q4FY23	Q4FY22	YoY (%)	Q3FY23	QoQ (%)
Revenue	**3,065**	**2,953**	**3.8**	**2,405**	**27.5**
Operating Expenses	2,909	2,835	2.6	2,294	26.8
Operating profit	**156**	**118**	**32.2**	**111**	**40.6**
Other Income	2	2	-	2.8	(35.5)
Interest	15	14	8.6	15	(0.2)
Depreciation	32	19	69.7	29	11.9
PBT	111	87	27.1	70	58.3
Tax	31	24	32.4	19	69.3
Reported PAT	81	63	27.7	52	55.4
Adjusted PAT	77	63	22.2	52	48.3
Adj. EPS (Rs.)	13.0	10.6	22.2	8.7	48.3
Margin			**bps**		**bps**
OPM (%)	5.1	4.0	110	4.6	48
NPM (%)	2.6	2.1	49	2.2	47
Tax rate (%)	28.5	27.3	115	26.0	246

Source: Company, Sharekhan Research

Segment-wise revenue and operating profit break-up (Rs. Crore) Rs cr

Particulars	Q4FY23	Q4FY22	YoY (%)	Q3FY23	QoQ (%)
Consumer Electronics	981	1,010	(3)	864	14
Lighting Products	270	305	(11)	263	3
Home Appliances	281	234	20	244	15
Mobile Phones	1,410	1,294	9	915	54
Security Systems	124	110	13	118	5
Total	**3,066**	**2,953**	**4**	**2,404**	**28**
Operating Profit					
Consumer Electronics	37	28	32	26	42
Lighting Products	26	22	18	24	9
Home Appliances	31	19	63	25	24
Mobile Phones	59	46	28	33	79
Security Systems	4	4	(5)	2.3	57
Total Operating Profit	**157**	**119**	**32**	**110**	**42**
OPM (%)			**BPS**		**BPS**
Consumer Electronics	3.8	2.8	100	3.0	(76)
Lighting Products	9.6	7.2	241	9.1	(54)
Home Appliances	11.0	8.1	292	10.2	(79)
Mobile Phones	4.2	3.6	63	3.6	(58)
Security Systems	2.9	3.5	(56)	1.9	(96)

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.

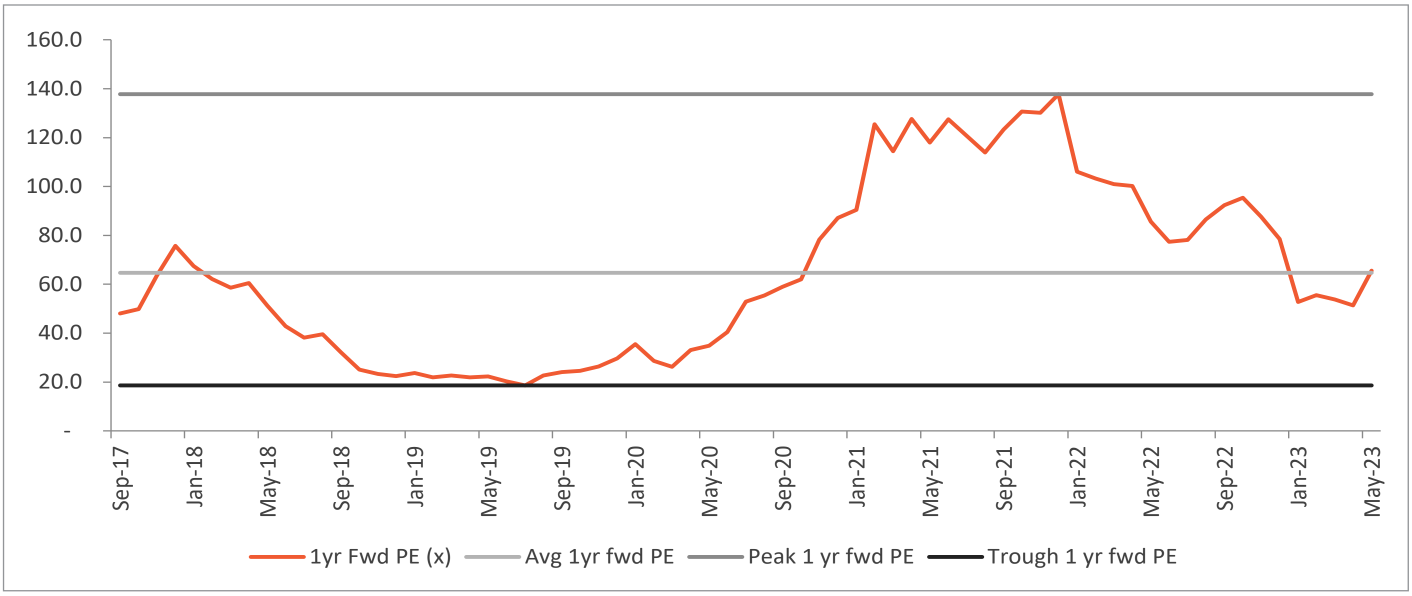
■ Company outlook - Healthy long-term outlook

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. In contrast, 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 - Maintain Hold with a revised PT of 4,050

Dixon Technologies has reported strong Q4 numbers and provided an optimistic outlook for FY24 without any specific revenue guidance. It has toned down its mobile revenue guidance to Rs. 6,000 crore in FY24 but expects to surpass it. We believe, 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. We expect sales/PAT CAGR of ~27%/39% over FY23- FY25E and margin expansion of ~25-30 bps to 4.5% over the same period. However, we await a better entry point for the investors given the expensive valuation as the stock trades at ~66xFY24E EPS and ~45xFY25E EPS. We also reckon that scalability in the mobile division holds the key to growth in the future. We value the stock on FY25E EPS and maintain Hold with a revised PT of Rs. 4,050.

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 ten 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 commissioning 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: Bloomberg

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Life Insurance Corporation of India	5.72
2	LIC ASM	5.00
3	Nippon Life India Asset Management	3.54
4	ICICI Prudential Life Insurance Company	3.29
5	Vanguard Group Incorporation	2.28
6	HDFC Asset Management Company	1.71
7	Kotak Mahindra Asset Management	1.68
8	Steadview Capital Mauritius	1.09
9	DSP Investment Managers Private	1.07
10	ICICI Prudential Asset Management	1.07

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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