Stock Update

Result Update

Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Dixon Technologies Ltd

Margin dents good revenue show, maintain Hold

Capital Goods	Sharekhan code: DIXON

Reco/View: Hold ↔	CMP: **Rs. 4,087**	Price Target: **Rs. 4,300** ↑

↑ 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 16.17

Updated Jul 08, 2023

Low Risk

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

Source: Morningstar

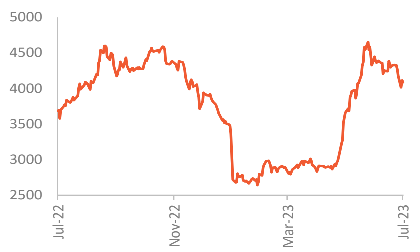
Company details

Market cap:	Rs. 24,256 cr
52-week high/low:	Rs. 4,730/2,553
NSE volume: (No of shares)	3.8 lakh
BSE code:	540699
NSE code:	DIXON
Free float: (No of shares)	3.9 cr

Shareholding (%)

Promoters	34.0
FII	15.0
DII	24.6
Others	26.4

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-6.3	45.2	22.3	9.3
Relative to Sensex	-10.9	35.2	12.1	-9.7

Sharekhan Research, Bloomberg

Summary

- Consolidated Q1FY24 performance was mixed as despite ~15% revenue growth, the company missed OPM estimates. Adjusted PAT growth was strong at 51% y-o-y.
- Management expects new customer additions, a robust order book in all key segments and scaling up of new verticals would drive growth.
- OPM are likely to expand owing to operating leverage, backward integration and an increase in revenue contribution through ODM solutions in consumer electronics and lighting segments.
- We have built-in revenue/earnings CAGR of 28%/42% (FY23-FY25E). We believe ramp up in its mobile division and traction in new verticals are the key growth catalysts. Currently, the stock trades at ~63x/~48x FY24/FY25E EPS. Given rich valuations, we continue to maintain Hold on Dixon with a revised PT of Rs 4,300.

Dixon Technologies Q1FY24 results were mixed as revenue was above estimates, but OPM missed estimates. Sales grew by 14.6% Y-o-Y to Rs. 3,272 crore (versus our expectation of Rs. 3,042 crore). The mobile & EMS division drove the revenue growth, which grew by 38% y-o-y to Rs. 1,795 crore. The operating profit for the quarter rose 32% y-o-y to Rs. 132 crore as against Rs 100 crore in the same quarter last year and in line with our expectations of Rs. 131 crore. OPM improved by 52 bps y-o-y to 4% but missed our expectations of 4.3%. The miss in the OPM results from low volumes in most of the key segments. Consolidated adjusted PAT for the quarter was Rs 69 crore against Rs 46 crore in the same period last year- a growth of ~51% (vs our estimate of Rs. 65 crore).

Key positives

- Strong revenue growth of ~38% in mobile & EMS division (~55% of total revenue).
- OPM in the mobile division were up by 40 bps y-o-y to 2.9%.
- Order book is strong in all key segments
- Debt/equity is low at 0.14 and net working capital is negative at 6 days.

Key negatives

- The margin missed the estimates as all key segments had soft volumes.
- The traditional lighting products are witnessing slowdowns and steep price corrections.
- LED TV demand is also weak, including Xiaomi and competitive intensity has also increased.

Management Commentary

- The company is confident of healthy growth in the long-term, which will be led by new customer additions mainly in mobile and consumer electronics segments
- The company would incur a capex of ~Rs.400-420 crore, directed mainly in the mobile followed by refrigerator and semi-auto washing machines. The company incurred a capex of Rs. 110 crore in Q1FY24.
- The company added Voltas Beko as its customer in consumer electronics. Demand for LED TV is muted. However, Dixon has maintained its market share. The TV volumes were 0.71mn vs. 0.74mn in Q1FY23
- Mobile division order book is strong in India, which is being driven by customer additions. The margin profile of this business would be somewhere in the range of 2.3% to 2.7%. For Xiaomi's phones, the capacity will be operational from September 2023 onwards.
- In mobile, the company added Itel as its customer - India's 5th largest smartphone company. Dixon would also be manufacturing Jio Bharat phones which is a huge long-term opportunity.
- In lighting, Dixon would also enter into products such as downlights, ceiling lights, ropes and other innovative products that are witnessing high demand and could aid revenue growth in the future.

Revision in estimates – We have marginally revised our revenue estimates for FY2024-25E to build in better revenue growth.

Our Call

Valuation – Maintain Hold with a revised PT of 4,300: Dixon Technologies has reported mixed numbers for Q1FY24 as it missed the margin estimates despite better-than-expected revenues driven by the mobile segment. We believe, in the long-term, Dixon could benefit from scaling up 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 ~28%/42% over FY23-FY25E and margin expansion of ~25-30 bps to 4.5% over the same period. However, we advise investors wait for a better entry point, given the expensive valuation as the stock trades at ~63x/~48x FY24/FY25E EPS. We maintain that scalability in the mobile division and expansion in new verticals holds the key to growth in the future. We value the stock on FY25E EPS and maintain Hold with a revised PT of Rs. 4,300.

Key Risks

- A slowdown in consumer discretionary spending and discontinuation or delay in the finalization of business from its key customers might affect revenue growth.
- Adverse raw-material prices, a delay in passing 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	16,901	20,061
OPM (%)	3.5	4.2	4.3	4.5
Adjusted PAT	190	252	389	506
% y-o-y growth	19.4	32.4	54.6	30.0
Adjusted EPS (Rs.)	32.1	42.3	65.4	85.0
P/E (x)	127.5	96.6	62.5	48.1
EV/EBITDA (x)	64.4	47.3	33.6	26.6
RoCE (%)	21.8	23.2	29.4	30.5
RoNW (%)	21.9	22.1	26.4	26.5

Source: Company Data; Sharekhan Research

Lower OPM weighs on Q1FY24 performance

Dixon Technologies Q1FY24 results were mixed as revenue exceeded estimates, but OPM missed estimates. Sales grew by 14.6% Y-o-Y to Rs. 3,272 crores (versus our expectation of Rs. 3,042 crores). The mobile & EMS division drove the revenue growth, which grew by 38% y-o-y to Rs. 1,795 crore. The operating profit for the quarter rose 32% y-o-y to Rs. 132 crore as against Rs 100 crore in the same quarter last year and in line with our expectations of Rs. 131 crore. OPM improved by 52 bps y-o-y to 4% but missed our expectations of 4.3%. The miss in the OPM results from low volumes in most key segments. Consolidated adjusted PAT for the quarter was Rs 69 crore against Rs 46 crore in the same period last year: a growth of ~51% (vs our estimate of Rs. 65 crore).

Q1FY2024 conference call highlights

- **Optimistic outlook:** The company is confident of healthy growth led by new customer additions, mainly in mobile and consumer electronics segments.
- **Capex Guidance:** The company would incur a capex of ~Rs.400-420 crore, directed mainly in the mobile, followed by refrigerators and semi-auto washing machines. The company incurred a capex of Rs. 110 crore in Q1FY24.
- **Consumer Electronics:** The company added Voltas Beko as its customer. The open cell prices went up to Rs. 12,000 vs Rs. 11,400 last year. Revenue in the segment was down 5% y-o-y, while OPM was up by 100 bps y-o-y to 3.4%. ODM's share in the total revenue increased to 30% vs 7% last year and the company expects it to increase to 40% by FY24. Demand for LED TV is muted. However, Dixon has maintained its market share. The TV volumes were at 0.71mn vs. 0.74mn in Q1FY23
- **Mobile division:** The revenue in the segment grew by 38% y-o-y to Rs.1,795 crore. OPM came in at 2.9%, up 40 bps y-o-y. The mobile order book is strong in India, driven by customer additions. The margin profile of this business would be somewhere in the range of 2.3% to 2.7%. Its capacity expansion in Noida would come on-stream by August 2023. For Xiaomi's phones, the capacity will be operational from September 2023 onwards. Motorola sales continue to be weak and were flattish at 1 mn units but the company expects a quarterly run rate of 1.4 mn units for the remaining FY24. The company added Itel as its customer, India's 5th largest smartphone company. The company would also be manufacturing Jio Bharat phones which is a huge opportunity.
- **Lighting:** Lighting revenue is down due to a significant value erosion in led bulb prices. However, due to the high ODM mix, OPM came in high at 8.7%, up 150 bps y-o-y. Dixon would also enter into products such as downlights, ceiling lights, ropes and other smart products which are witnessing high demand and could aid revenue growth going forward. Also, exports opportunity to the tune of Rs. 100 crore exists in markets like the US, Europe and UAE markets. The company is also focusing on the professional lighting segment, which is a substantial part of the entire lighting industry. It expects to launch products in this vertical by Q4FY24.
- **IT hardware:** The government has recently announced a revised PLI scheme for IT hardware products with a higher incentive payout and Dixon will be participating in the same. For this purpose, the company is in discussions with some large global brands. Currently, the company's focus is notebooks, which could also be extended to desktops and tablets.

Results (Consolidated) **Rs cr**

Particulars	Q4FY23	Q4FY22	YoY (%)	Q3FY23	QoQ (%)
Revenue	**3,272**	**2,855**	**14.6**	**3,065**	**6.7**
Operating Expenses	3,140	2,755	14	2,909	7.9
Operating profit	**132**	**100**	**31.7**	**156**	**-15.6**
Other Income	3	0	578.6	1.8	56.6
Interest	14	14	-3	15	-7.5
Depreciation	34	24	40.1	32	3.9
PBT	87	62	40.2	111	-21.3
Tax	23	17	38.1	31	-27.4
Reported PAT	67	45	47.9	81	-16.7
Adjusted PAT	69	46	50.6	77	-10.6
Adj. EPS (Rs.)	11.6	7.7	50.6	13	-10.6
Margin			**bps**		**bps**
OPM (%)	4.0	3.5	52	5.1	-107
NPM (%)	2.1	1.6	46	2.6	-58
Tax rate (%)	26.3	26.7	-39	28.5	-222

Source: Company Data; 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 proliferating. 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.

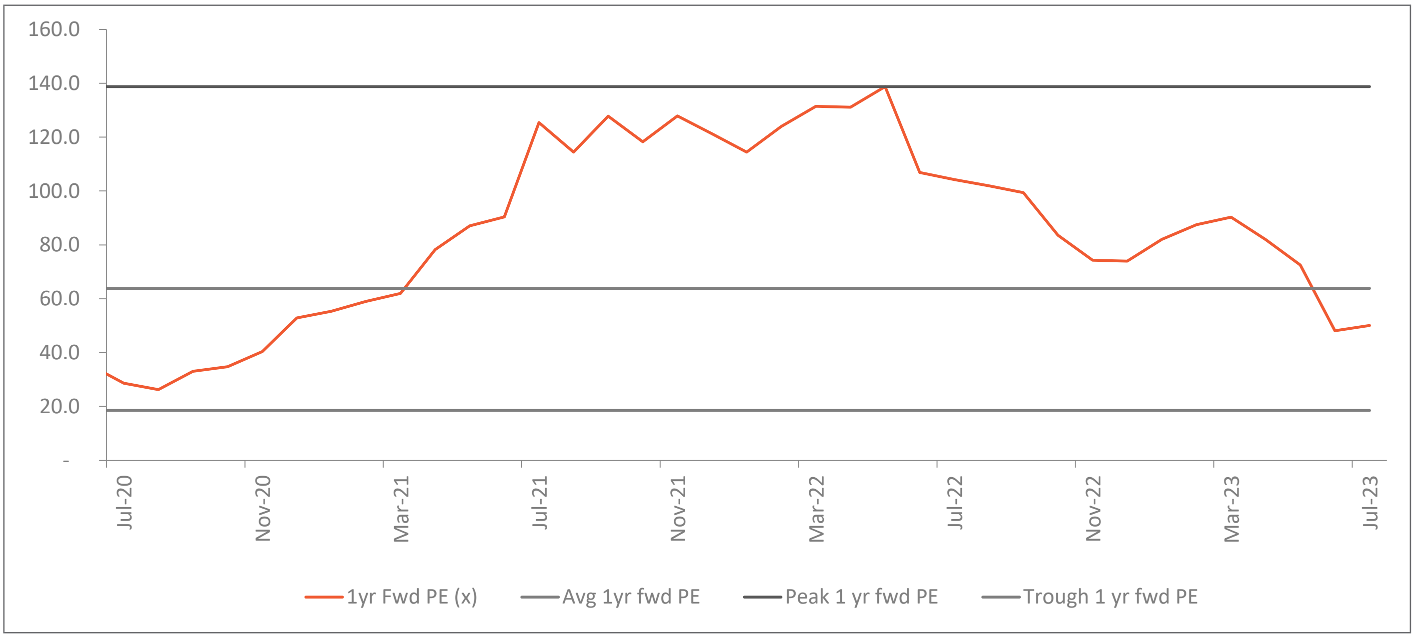
■ Company Outlook – Client addition and margin expansion would be key growth catalysts

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, will likely drive revenue growth momentum. In contrast, the margin may expand due to the lighting business's economies of scale and automation. 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 4,300

Dixon Technologies has reported mixed numbers for Q1FY24 as it missed the margin estimates despite better-than-expected revenues driven by the mobile segment. We believe, in the long-term, Dixon could benefit from scaling up 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 ~28%/42% over FY23-FY25E and margin expansion of ~25-30 bps to 4.5% over the same period. However, we advise investors wait for a better entry point, given the expensive valuation as the stock trades at ~63x/~48x FY24/FY25E EPS. We maintain that scalability in the mobile division and expansion in new verticals holds the key to growth in the future. We value the stock on FY25E EPS and maintain Hold with a revised PT of Rs. 4,300.

One-year forward P/E (x) band



Source: Company Data; Sharekhan Research

About the company

Founded by Mr 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 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 the 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, a 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	5.7
2	LIC ASM	5.0
3	Nippon Life India Asset Management	2.6
4	ICICI Prudential Life Insurance	2.4
5	HDFC Asset Management	2.0
6	Vanguard Group Incorporation	1.9
7	Kotak Mahindra Asset Management	1.9
8	PGIM India Asset Management	1.2
9	Steadview Capital Mauritius	1.1
10	DSP Investment Managers	1.0

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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