February 16, 2017

Dixon Technologies India Private Limited

Instrument*	Rated Amount (in crore)	Rating Action
Commercial Paper	25.0	[ICRA]A1; Assigned

Instrument Details are provided in Annexure-1

Rating Action

ICRA has assigned a short-term rating for the Rs. 25.0-crore[1] commercial paper programme of Dixon Technologies India Pvt. Ltd. (DTIPL) at [ICRA]A1 (pronounced as ICRA A one)[2]. ICRA also has a long-term rating of [ICRA]A (pronounced ICRA A) with a stable outlook for the Rs. 15.3-crore bank facilities and a short-term rating of [ICRA]A1 (pronounced as ICRA A one) for the Rs. 119.7-crore bank facilities of DTIPL.

Detailed Rationale

The rating factors in DTIPL's healthy scale of operations, improving operating profitability, and modest working capital intensity which resulted in low dependence on external borrowings and comfortable credit metrics. The rating also factors in the expected improvement in DTIPL's operating profitability as it is gradually shifting towards higher value-added product offering, and also due to traction in its higher-margin refurbishing business. The rating action positively factors in the conversion of convertible debentures (held by the external investors) into equity shares in FY2017, thereby improving the net worth of the company and also eliminating the risk of any debt-funded exit provided by the company. The rating also considers the promoter's long experience and track record in electronic manufacturing services (EMS) business, its reputed clientele, diversified product portfolio, and the company's presence in excise-free zone.

The rating is, however, constrained by concentration of DTIPL's revenues among few customers, which makes it dependent on the business plans and performance of its key customers. In the recent past, one of DTILPL's large customers (Toshiba) had changed its India-related business plans, resulting in loss of business volumes from this customer, though DTIPL was able to reduce the impact by adding new customers. ICRA has taken comfort from the long relationship with its key clients and their strong financials and market positions. The rating also factors in limited period of excise duty exemption, uncertainty regarding the excise exemptions post implementation of Goods and Services Tax (GST) and sustainability of its profitability post the expiry of the excise duty exemptions. Nevertheless, ICRA believes that DTIPL will remain competitive with its lean cost structure, long track record, and ability to adapt with the rapid technology upgradation in the consumer electronics/durable space which requires continuous process alterations and improvements.

ICRA has also factored in DTIPL's capex plans to enhance value addition and capacities; however, these are to be funded primarily from the internal accruals. In case of DTIPL using sizeable debt to fund capex, the credit metrics could get impacted and would remain a key rating sensitivity. Apart from these, the company's ability to diversify its client base, scale up its operations, improve its profitability and debt coverage indicators will be the key rating sensitivities. DTIPL's ability to maintain its profitability post expiry of the excise duty exemptions will also be a key rating sensitivity.

[1] 100 lakh = 1 crore = 10 million

[2] For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications

Key rating drivers

Credit Strengths

- Long presence in contract manufacturing business, experience of its promoters and relationships built by them in this field
- Stable volumes from its existing principals (like Panasonic, Philips), and addition of new principals
- Improvement in financial profile with healthy revenue growth, better operating profitability, and limited dependence on external borrowings resulting in an improvement in credit metrics
- Expected improvement in operating profitability with more contribution coming from higher-margin ODM (original design manufacturer) products and refurbishment of set-top box business
- Conversion of convertible debentures into equity shares, thereby improving the net-worth of the company and also eliminating the risk of any debt-funded exit provided by the company

Credit Weaknesses

- Dependence on business plans and performance of its customers as consumer electronics is a very dynamic segment. This has been demonstrated with outgoing customers like Toshiba, ELCOT, and products like CTV, MP3 player etc. Despite long relationships, the ability to get continuous business is limited to the performance and plan of the client and the technology involved.
- High concentration of revenues from Philips and Panasonic; however, both the companies are global players with strong financial profile
- DTIPL enjoys competitive advantage in terms of excise duty exemptions. However, post implementation of GST, there is uncertainty whether these exemptions would continue. Competition from other assembly players and in-house capacities of brands, particularly post the expiry of excise duty exemptions, remain a challenge.
- Risk of obsolescence of product necessitates the need to continuously upgrade and diversify. The company has taken steps to diversify into new products like washing machines, mobile phones etc.

Description of key rating drivers highlighted above:

DTIPL is a leading player in the Indian electronic contract manufacturing space and has established relationships with consumer electronic majors. However, as prevalent in such an industry, the company's revenues are linked to the business plan and performance of its customers. The company needs to make continuous efforts to maintain its cost competitiveness in addition to bring out new products given the dynamic nature of the product segment. Further, access to cheap labour, given the labour-intensive nature of operations and tax benefits enjoyed at present at its facilities, are the key factors determining its cost competitiveness.

LED and LCD TV segment is one of the strongest and the largest segments in terms of revenues at present. Earlier, DTIPL was undertaking assembly of CTVs mainly for LG and other players. With the phasing out of CTVs, DTIPL moved into LCD/LED TV segment. This segment grew rapidly during FY2013-FY2015. However, during FY2016, the overall volumes in this segment remained stagnant as one of its large clients - Toshiba - had discontinued its Indian operations. The loss of volumes from Toshiba was partly compensated by strong growth from Panasonic, and addition of new customers.

DTIPL has a long-term strategy of becoming an original design manufacturer (ODM) wherein it will supply an entire product starting from design. In the medium term, to improve upon the margins, DTIPL is focusing on increasing value addition in its offerings and plans to become a CKD (completely knocked down) assembler from the current semi knocked down (SKD) assembler. This is expected to improve margins and is a logical related diversification path. For this, the company is adding new assembly lines on an adjacent land bank that it has.

DTIPL had issued compulsorily convertible debentures (CCD) of Rs. 37.5 crore in FY2009-FY2010 to Private Equity (PE) investors. While, these CCDs had a compulsory conversion period after 10 years of issuance, investors had converted these Convertible Debentures into equity shares in August 2016. From credit perspective, the conversion into equity shares has reduced concerns related to the liability to buyback debentures falling upon the company. Furthermore, this has improved the Dixon's net-worth.

Most of DTIPL's operations are located in excise-free zones in Dehradun (Uttarakhand). As a result, it has the advantage of paying lower overall excise duty. This gives DTIPL cost competitiveness against its competitors and also cost advantage to its clients. As per the excise free zone condition, the excise duty exemptions would lapse across the country after 2020. With the implementation of GST from April 2017, there remains uncertainty on the continuation of excise exemptions to the companies in the excise-free zones. DTIPL being the largest player in this business and having built long association with clients, is expected to enjoy an edge over the competition even after the excise benefits lapse. However, the intensity of competition is likely to increase which could impact profitability.

DTIPL's ability to sustain its working capital intensity at lower levels has been a key rating sensitivity. Lower funding requirement in the LED TV assembly segment (due to shorter receivable period) enables it to maintain its working capital cycle efficiently. Despite high growth in operating income, the company has been able to manage its working capital efficiently, resulting in lower dependence on external borrowings. While the company has capital expenditure plans, the same would be funded through internal accruals and the debt levels are not expected to increase significantly over the medium term.

Analytical approach: Not applicable

Links to applicable Criteria:
Corporate Credit Rating –A Note on Methodology

About the Company:
Dixon Technologies (India) Private Limited (DTIPL), incorporated in 1993 by Mr. Sunil Vachani, is involved in the manufacturing of consumer durables which comprise mainly televisions, lighting products (CFL, LEDs, ballasts), and washing machines. The company operates as a contract manufacturer for consumer electronics majors like Philips, Panasonic etc. DTIPL has manufacturing facilities in Noida (Uttar Pradesh) and Dehradun (Uttarakhand), which have capacities for assembly of Printed Circuit Boards (PCB), CTVs, LED/LCD TVs, ballasts, CFLs, LEDs, set-top boxes, washing machines, energy meters etc. Recently, the company has entered into a joint venture with Jaina Group for manufacturing of mobile phones in Noida.

DTIPL has two key subsidiaries – Dixon Appliances Pvt. Ltd. (DAPL), Dixon Bhurji Moulding Pvt. Ltd. (DBMPL), and Dixon Global Pvt. Ltd. (DGPL) which will be amalgamated with it. DAPL manufactures washing machines and allied products while DBMPL is backwardly integrated to DTIPL and manufactures moulding and sheet metal parts. This apart, DTIPL has recently entered into joint venture (50% each) – Padget Electronic Pvt Ltd – with Jaina Group for mobile handset manufacturing.

During FY2009-FY2010, M/s India Business Excellence Fund 1 and IL&FS Trust Company Ltd had invested Rs. 37.5 crore into convertible debentures. In August 2016, DTIPL's board had approved conversion of these convertible debentures into equity shares. Post this conversion, the two investors together hold 32.2% shareholding in the company.

As per the financials for the first half of the current financial year (H1FY2017), DTIPL (on a consolidated level) had an operating income (provisional) of Rs. 1,168.9 crore and a profit before tax of Rs. 35.5 crore. In FY2016, on a consolidated basis, the company reported an operating income of Rs. 1,388.3 crore and a net profit of Rs. 27.4 crore.

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History for last three years:

Table: Rating History

Name of Instrument	**Current Rating**			**Chronology of Rating History for the past 3 years**				
	Type	**Rated amount (Rs. Crore)**	**Month-year & Rating**	**Month-year & Rating in FY2017**	**Month-year & Rating in FY2016**	**Month-year & Rating in FY2015**	**Month-year & Rating in FY2014**	**Month-year & Rating in FY2014**
			February 2017	**September 2016**	**January 2016**	**January 2015**	**Mar 2014**	**May 2013**
New Rating Assigned								
Commercial Paper	Short Term	25.0	[ICRA]A1	-	-	-	-	-
Existing Rating								
Term Loans/Non-fund based	Long Term	15.3	[ICRA]A	[ICRA]A	[ICRA]A-	[ICRA]BBB+	[ICRA]BBB	[ICRA]BBB-
			Stable	Stable	Stable	Stable	Stable	Positive
Fund Based/Non-fund based/ unallocated	Short Term	119.7	[ICRA]A1	[ICRA]A1	[ICRA]A2+	[ICRA]A2	[ICRA]A3+	[ICRA]A3

Complexity level of the rated instrument:

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1

Details of Instrument

Name of the instrument	Date of issuance	Coupon rate	Maturity Date	Size of the issue (Rs. Cr)	Current Rating and Outlook
New Rating Assigned					
Commercial Paper	*	*	*	25.0	[ICRA]A1
Existing Ratings					
Term Loan	-	-	FY2021	13.3	[ICRA]A (Stable)
Non-fund based	-	-	-	2.0	[ICRA]A (Stable)
Short term fund based	-	-	-	69.0	[ICRA]A1
Short term non-fund based	-	-	-	50.0	[ICRA]A1
Unallocated	-	-	-	0.7	[ICRA]A1

*Not placed as of January 31, 2017

Source: DTIPL

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ICRA

About ICRA Limited:
ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.
Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.
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