

November 25, 2020

Dixon Technologies (India) Limited (erstwhile Dixon Technologies (India) Private Limited): Long-term rating upgraded and outlook revised to Stable; short-term rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based -Term Loan	52.70	52.70	[ICRA]AA- (Stable); Upgraded from [ICRA]A+ (Positive), outlook revised to 'Stable' from 'Positive'
Fund-based - Working Capital Facilities	145.00	145.00	[ICRA]A1+; Reaffirmed
Non-fund Based - Working Capital Facilities (Short-term scale)	635.00	635.00	[ICRA]A1+; Reaffirmed
Interchangeable^ Working Capital Facilities (Short-term scale)	250.00	250.00	[ICRA]A1+; Reaffirmed
Unallocated Bank facilities (Short-term scale)	47.34	47.34	[ICRA]A1+; Reaffirmed
Commercial Paper	100.00	100.00	[ICRA]A1+; Reaffirmed
Total	1230.04	1230.04	

[^] between non-fund based and fund based, *Instrument details are provided in Annexure -1

Rationale

The rating upgrade takes into account robust performance of Dixon Technologies (India) Limited (DTIL) in the recent past, as well as the expected significant increase in its scale of operations with the receipt of approval of its subsidiary's application under the Production Linked Incentive (PLI) scheme by the Ministry of Electronics and Information and Technology (MeitY). Despite the disruption in operations due to the Covid-19 pandemic-related lockdown, DTIL has witnessed strong recovery in business post easing of Covid-19-related curbs as reflected in the 17% YoY growth in revenues along with an improvement in the operating profitability in Q2 FY2021. The ratings continue to take into account the healthy operating profile of DTIL, characterised by its established track record as an electronic manufacturing services (EMS) player with presence in diversified product segments, leading position in its key product segments (like LED television, lighting, etc.) and its well-established relationship with reputed clientele. The ratings also consider DTIL's healthy financial profile characterised by moderate leverage, strong return on capital employed, and healthy debt coverage indicators. Further, the ratings positively take into account the backward-integration measures in its key business segments, which have supported its growth and profitability improvement over the years.

The long-term rating, however, is constrained by DTIL's dependence on a few large clients, which renders its revenues susceptible to the business plans and performance of the same. Further, the revenue concentration has reduced over the years, with business from the top three clients reducing to 58% in H1 FY2021 from 71% in

FY2018. However, the strong profile of the large principals—Xiaomi – Moody’s Baa2 (Stable) and Samsung – Moody’s Aa3 (Stable)—and DTIL’s position as one of the largest and cost-efficient EMS players in India, partially abates the risk of business loss from any large client. The rating also factors in the competitive and dynamic nature of the electronics manufacturing industry, which exposes the players to risk of technological obsolescence, foreign exchange fluctuation and regulatory changes. This in turn necessitates continuous upgrade of processes and products to sustain competitive advantage, requiring regular capital expenditure. DTIL, like other electronics manufacturers, has a high dependence on imported raw materials/components and is susceptible to any significant supply-chain disruption.

DTIL’s operations have sizeable working capital requirements (both fund-based and non-fund based) due to lead time in imports and receivables realisation period, and the same gets funded to a large extent by the credit period from suppliers, resulting in relatively high total outside liabilities/ tangible net worth (TOL/TNW) ratio and dependence on sizeable non-fund based limits (letter of credit or LC). However, ICRA has noted that part of DTIL’s creditors are covered by bank guarantees, which reduces the credit risk. Additionally, DTIL enters into back-to-back payment arrangement with some of its suppliers, who are either a related party to its principals or are identified by them; this mechanism, while lowering DTIL’s working capital requirements as well as credit risks, also results in creation of debtor and creditor for DTIL from the same/related parties. In the past, DTIL was allowed to knock-off both debtors and creditors related to Gionee transactions when the latter got into financial trouble. Taking the same into cognisance, ICRA has adjusted such creditors as well as netted off lease obligations, cash balances and liquid investments from its TOL for evaluating adjusted TOL/TNW ratio. The adjusted TOL/TNW ratio for the company was comfortable at 1.8 times as of September 30, 2020. The financial metrics of DTIL, however, remain critically dependant on the prudent management of its working capital requirements. In this context, ICRA takes comfort from the company’s past track record, its healthy liquidity position and financial flexibility.

The Stable outlook on the rating reflects ICRA’s expectation that DTIL will continue to report a healthy growth in its scale of operations, along with diversification in customer profile, product profile and supply chain.

Key rating drivers and their description

Credit strengths

Established track record and market position in EMS business – DTIL has more than two decades of experience in the EMS business and has an established track record and leadership position in the key segments in which it operates, i.e. LED television, lighting, and washing machine. Over the years, the company has augmented its manufacturing capacities alongside acquiring cost competency to become one of the largest and cost-efficient EMS players in the country. These strengths have helped DTIL in adding new principals as well as maintaining healthy relationship with its clients, resulting in repeat business.

Diversified revenue streams across product segments with reputed clientele – The company’s revenues are diversified across product segments like consumer electronics (CE; mainly LED television), lighting, home appliances (mainly washing machines), mobiles and security devices. In FY2021, the company has ventured into manufacturing of set-top boxes and medical electronics. While the CE, lighting, and home appliances segments are catered to by DTIL, mobile phone and medical electronics manufacturing comes under its subsidiary, Padget Electronics Private Limited (erstwhile JV), and security devices and set-top boxes manufacturing is undertaken under the subsidiary company AIL Dixon Technologies Private Limited (JV with Aditya Infotech Limited),

respectively. The presence across multiple product segments provides DTIL a diversified revenue stream and growth opportunities across segments. The company's clientele comprises some strong and reputed global brands like Xiaomi, Samsung, Panasonic, Phillips, etc. The addition of a new clientele has also supported supply chain diversification.

Healthy financial profile with moderate leverage and healthy debt coverage metrics – DTIL's financial profile remains healthy with robust improvement in Q2 FY2021, despite a challenging environment, supported by increased volumes in the CE vertical, profitability improvement supported by backward integration, moderate leverage and healthy debt coverage indicators. The company's net worth has also improved on the back of healthy accruals from operations and issuance of employee stock option programme; while external borrowing has remained limited. The credit profile remained healthy as reflected in interest coverage ratio of 8.4 times and debt service coverage ratio of 6.0 times in H1 FY2021. The liquidity position remains comfortable with adequate cushion in fund-based working capital limits. While the nationwide lockdown and labour/logistic challenges had impacted its performance in Q1 FY2021, the performance improved in Q2 FY2021 supported by a robust recovery since June 2020. One of DTIL's subsidiaries—Padget Electronics Private Limited—had made an application under the PLI scheme that was approved by the MeitY in October 2020. This is expected to provide significant boost to DTIL's scale of operations and profits, given the incentive available under the scheme. The company plans to undertake debt-funded capex that would increase its long-term borrowings. However, its increased scale and profitability is expected to keep its coverage profile healthy.

Credit challenges

Dependence on customers' business plans and performance; however, strong patronage of key principals abates associated risks to an extent – As is prevalent in the industry, the company's revenues are closely linked to the business plan and performance of its principals. A major part of DTIL's revenues and operating profitability is derived from its top three customers—Xiaomi, Samsung and Panasonic. However, ICRA derives comfort from the company's long relationship with its top clients (Panasonic – over five years) and strong patronage of the clients. While the risks of customer loss and product obsolescence remain, the company has a demonstrated track record of withstanding such losses in the past. Nevertheless, it needs to make continuous efforts to maintain its cost competitiveness and upgrade to new products, given the dynamic nature of the product segment. Despite its long-standing relationships, the company's ability to get repeat business is linked to the performance and plan of the clients and the technology involved.

Competition and risk of technological obsolescence necessitates continuous upgrade of processes and products – The consumer durable/electronic products/EMS industry is characterised by continuous product and process innovation and rapid adoption of new technology. Given the risk of technological obsolescence, the industry players are required to undertake continuous upgrades to sustain competitive advantage. The company faces competition from other EMS players, besides exposure to in-house capacities of brands. These limit its pricing flexibility and bargaining power with customers, thereby putting pressure on margins in segments like CE and mobiles, which face relatively more competition. The competition has increased following the entry of globally competitive contract manufacturing players in the domestic market in the recent years. Further, the company is exposed to risks pertaining to regulatory changes (like custom duty, taxation, etc.) and foreign exchange exposure, given its sizeable imports. However, the forex risk is abated to an extent with the company's ability to partly pass on the variation.

High TOL/TNW due to high creditors and working capital requirements; however, adjusted TOL/TNW ratio remains comfortable – DTIL's business calls for sizeable dependence on supplier's credit, though most of these have back-to-back arrangements with the corresponding clients. The company's operations require sizeable working capital limits (fund-based and non-fund based). It imports over 60% of its raw material/component requirements. A sizable portion of these imports are backed by usance LCs. Typically, the usance period covers the cash conversion cycle, i.e. the lead time in imports and receivables, production, and realisation period. Therefore, at any given point in time, the company has sizable utilisation of non-fund based limits. Further, it utilises fund-based facilities like bill discounting and other working capital borrowings to meet its working capital requirements. There is an empirical mild cyclical in working capital requirement, given the high sales of electronic products near the festive season, resulting in higher TOL during the middle of a financial year. However, ICRA has noted that part of the creditors are covered by bank guarantees, which reduces the risk. Additionally, some creditors are related party to the client and have back-to-back arrangements between receivables and payables. ICRA has adjusted such creditors as well as netted off lease obligations, cash balances and liquid investments from the TOL for evaluating adjusted TOL/TNW ratio. The adjusted TOL/TNW ratio for the company was comfortable at 1.8 times as of September 30, 2020.

The financial metrics of DTIL remain critically dependant on prudent management of its working capital requirements. In this context, however, ICRA takes comfort from the company's track record and its healthy liquidity position and financial flexibility.

Liquidity position: Adequate

DTIL has healthy cash generation from operation, which is reflected in the healthy and increasing fund flow from operations (FFO) of the company. The liquidity is further supported by the free cash balance of Rs. 69.9 crore and undrawn fund-based limits of Rs. 177.6 crore as on September 30, 2020. The company plans to undertake debt-funded capex in FY2021–FY2024, which is expected to increase repayment obligation from FY2022 onwards; however, the scale of operations and cash flows are also expected to increase significantly. Thus, the liquidity position is expected to remain **adequate** with the healthy cash generation and limited scheduled debt repayment.

Rating sensitivities

Positive triggers – A rating upgrade is unlikely in the near term. The outlook on the rating maybe revised to Positive if the company is able to maintain the pace of revenue growth while achieving sustainable improvement in profitability and greater customer diversification alongside improvement in financial profile. Specific credit metrics that could lead to an upgrade of Dixon's rating include adjusted net TOL/ TNW[^] below 1.25 times on a sustainable basis.

Negative triggers – The ratings maybe downgraded if the loss of any large client or slowdown in its key product segments materially affects DTIL's financial performance. The ratings may also be downgraded if any increase in working capital intensity or decline in profitability results in tightening of the liquidity position or stretching payables leads in an increase in leverage to adjusted net TOL/TNW of over 2.0 times on a sustained basis. The rating may also be downgraded in case of supply chain disruption materially affecting the company's financial performance.

[^]*Adjusted net TOL/TNW ratio: For arriving at adjusted net TOL/TNW, the TOL has been adjusted by netting off lease obligations, cash balances and liquid investments, and creditors which are either covered by BGs or where*

clients and suppliers are related parties. Notably, DTIL has irrevocable BGs from one of the principles, that overcomes any counterparty risk and therefore reduces the TOL to the extent covered by the outstanding within the BG coverage. Further another principle has an associated supplier. These liabilities have been adjusted from TOL for arriving at the adjusted ratio.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology
Parent/Group Support	Not applicable
Consolidation/Standalone	The rating is based on consolidated financial statements of the issuer, which includes its subsidiaries and JVs

About the company

Dixon Technologies (India) Limited (DTIL), incorporated in 1993 by Mr. Sunil Vachani, is a diversified EMS company with operations in various subsegments of the electronic products vertical. DTIL has operations in consumer electronics, lighting, home appliance, and mobile phone segments and also undertakes reverse logistics operations. Besides, the company undertakes manufacturing of security surveillance equipment through a JV company.

TV manufacturing, part of the CE vertical, has been the largest segment for DTIL over the years. The company has, over the last couple of years, added new principles in the segment. This in turn has supported growth in segmental volumes and revenues. In the home appliances segment, the company has a range of 100% original design manufacturing (ODM) products. This segment, along with and its backward integration in the lighting segment, has supported profitability improvements in the recent years. DTIL ventured into mobile phone manufacturing in 2016 through a JV (50%) Padget Electronic Pvt. Ltd. with the Jaina Group. DTIL consolidated its shareholding in the company with the acquisition of the JV partner's share in April 2019. Thereafter, PEPL become its wholly-owned subsidiary. In January 2018, it entered into manufacturing of surveillance and security equipment like closed-circuit television cameras (CCTVs) and digital video recording (DVR) through AIL Dixon Technologies Private Limited, its 50% JV with Aditya Infotech Ltd. DTIL has manufacturing facilities in Noida, Dehradun, and Tirupati. The company has recently received an approval under the PLI scheme as a domestic manufacturer of mobile phones. In September 2017, the company came out with an IPO worth ~Rs. 600 crore, which involved ~Rs. 60 crore of fresh equity issuance and the remaining as offer for sale from promoter/investors.

In FY2020, the company reported a net profit of Rs. 120.5 crore on an OI of Rs. 4,400.1 crore compared to a net profit of Rs. 63.4 crore on an OI of Rs. 2,984.4 crore in the previous year. In H1 FY2021 the company reported a net profit of Rs. 54.0 crore on an OI of Rs. 2,155.7 crore.

Key financial indicators (audited)

	FY2018	FY2019	FY2020	H1FY2021
Operating Income (Rs. crore)	2,841.6	2,984.4	4,400.1	2155.7
PAT (Rs. crore)	60.9	63.4	120.5	54.0
OPBDIT/OI (%)	4.0%	4.6%	5.2%	4.9%
RoCE (%)	30.4%	23.2%	29.8%	23.8%
Total Outside Liabilities/Tangible Net Worth (times)	2.4	3.2	2.3	3.0
Total Debt/OPBDIT (times)	1.2	1.8	0.8	0.9
Interest Coverage (times)	8.0	5.2	5.8	8.4
DSCR	5.2	3.8	4.3	6.0

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Instrument	Type	Rating (FY2021)		Amount Outstanding As on 30-Sep-20	Current Rating 25-Nov-2020	Earlier Rating 28-Sep-2020	01-May-2020	Rating History for the Past 3 Years					
		Amount Rated						FY2020			FY2019		FY2018
								11-Oct-2019	3-Oct-2019	10-Jun-2019	1-Mar-2019	20-Sep-2018	6-Oct-2017
1 Commercial Paper	Short Term	100.00	50.00		[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
2 Fund-based -Term Loan	Long Term	52.70	37.30		[ICRA]AA-(Stable)	[ICRA]A+(Positive)	[ICRA]A+(Stable)	[ICRA]A+(Stable)	[ICRA]A+(Stable)	[ICRA]A+(Stable)	[ICRA]A+(Stable)	[ICRA]A+(Stable)	[ICRA]A+(Stable)
3 Fund-based - Working Capital Facilities	Short Term	145.00	-		[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
4 Non-fund Based - Working Capital Facilities	Short Term	635.00	-		[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
5 Interchangeable^ Working Capital Facilities	Short Term	250.00	-		[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	-
6 Unallocated Bank facilities	Short Term	47.34	-		[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	-	-	-	-

Amount in Rs. Crore

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: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Commercial Paper*	NA	NA	7-365	100.00	[ICRA]A1+
NA	Fund-based -Term Loan 1	18-Nov-2015	NA	31-Dec-2020	2.70	[ICRA]AA- (Stable)
NA	Fund-based -Term Loan 2	20-Jan-2020	NA	31-Jan-2026	50.00	[ICRA]AA- (Stable)
NA	Fund-based - Working Capital Facilities	NA	NA	NA	145.00	[ICRA]A1+
NA	Non-fund Based - Working Capital Facilities	NA	NA	NA	635.00	[ICRA]A1+
NA	Interchangeable^ Working Capital Facilities	NA	NA	NA	250.00	[ICRA]A1+
NA	Unallocated Bank facilities	NA	NA	NA	47.34	[ICRA]A1+

* Amount placed is Rs. 50.00 crore as on 22-Sep-20; ^ between non-fund based and fund based, Source: DTIL

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Dixon Global Private Limited	100.00%	Full Consolidation
Padget Electronics Private Limited*	100.00%	Full Consolidation
AIL Dixon Technologies Private Limited	50.00%	Proportionate Consolidation Method/ Equity Method

* The ownership has increased from 50% to 100% in Q1-FY2020

Analyst Contacts

Shubham Jain

+91 124 4545 306

shubhamj@icraindia.com

Abhishek Gupta

+91 124 4545 863

abhishek.gupta@icraindia.com

Nitin Kumar

+91 124 4545 845

nitin.kumar2@icraindia.com

Relationship Contact

Jayanta Chatterjee

+91 80 4332 6401

jayantac@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani

Tel: +91 124 4545 860

communications@icraindia.com

Helpline for business queries:

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

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.

For more information, visit www.icra.in

ICRA Limited

Corporate Office

Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002

Tel: +91 124 4545300

Email: info@icraindia.com

Website: www.icra.in

Registered Office

1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001

Tel: +91 11 23357940-50

Branches

Mumbai + (91 22) 24331046/53/62/74/86/87
Chennai + (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,
Kolkata + (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,
Bangalore + (91 80) 2559 7401/4049
Ahmedabad+ (91 79) 2658 4924/5049/2008
Hyderabad + (91 40) 2373 5061/7251
Pune + (91 20) 2556 0194/ 6606 9999

© Copyright, 2020 ICRA Limited. All Rights Reserved.

Contents may be used freely with due acknowledgement to ICRA.

ICRA ratings should not be treated as recommendation to buy, sell or hold the rated debt instruments. ICRA ratings are subject to a process of surveillance, which may lead to revision in ratings. An ICRA rating is a symbolic indicator of ICRA's current opinion on the relative capability of the issuer concerned to timely service debts and obligations, with reference to the instrument rated. Please visit our website www.icra.in or contact any ICRA office for the latest information on ICRA ratings outstanding. All information contained herein has been obtained by ICRA from sources believed by it to be accurate and reliable, including the rated issuer. ICRA however has not conducted any audit of the rated issuer or of the information provided by it. While reasonable care has been taken to ensure that the information herein is true, such information is provided 'as is' without any warranty of any kind, and ICRA in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness or completeness of any such information. Also, ICRA or any of its group companies may have provided services other than rating to the issuer rated. All information contained herein must be construed solely as statements of opinion, and ICRA shall not be liable for any losses incurred by users from any use of this publication or its contents