

August 26, 2022

Dixon Technologies (India) Limited: Ratings reaffirmed; rated amount enhanced

Summary of rating action

| Instrument* | Previous Rated Amount (Rs. crore) | Current Rated Amount (Rs. crore) | Rating Action |
|--|--------------------------------------|-------------------------------------|---|
| Commercial paper | 175.00 | 175.00 | [ICRA]A1+; Reaffirmed |
| Fund-based -Term loan | 52.70 | 240.00 | [ICRA]AA- (Stable); Reaffirmed and Assigned for enhanced limits |
| Fund-based - Working capital facilities | 145.00 | 650.00 | [ICRA]A1+; Reaffirmed and Assigned for enhanced limits |
| Non-fund Based - Working capital facilities (short-term) | 1,345.00 | 1,735.00 | [ICRA]A1+; Reaffirmed and Assigned for enhanced limits |
| Unallocated bank facilities (short-term) | 47.34 | - | - |
| Total | 1,765.04 | 2,800.00 | |

*Instrument details are provided in Annexure I

Rationale

The ratings factor in the robust growth in Dixon Technologies (India) Limited's (DTIL) scale of operations in the recent past (at a five-year CAGR of 34%), which imparts economies of scale benefit. The ratings take into account DTIL's 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 favourably factor in DTIL's strong return on capital employed (RoCE) and comfortable debt coverage indicators with an interest cover of 7.8 times in FY2022. The ratings also note the healthy ramp-up in the mobile phone segment, which received approval under the Indian Government's Production Linked Incentive (PLI) scheme. Though the revenue is expected to increase over 25% in FY2023, operating margins are expected to sustain at the current levels. The company has achieved the capex and revenue targets for the first year and has applied for the incentives. Further, the ratings positively consider the backward-integration measures in the company's key business segments, which have supported its growth and profitability over the years.

The ratings, however, are constrained by DTIL's leveraged capital structure with net TOL¹/TNW of 3.3 times as of March 2022 and dependence on a few large clients, which exposes its revenues to the business plans and performance of the same. It has sizeable working capital requirements (both fund-based and non-fund based) due to the lead time in imports and receivables realisation period. The same gets funded, to a large extent, by the credit period from suppliers. This results in a relatively high TOL/TNW ratio and dependence on sizeable non-fund based limits (letter of credit or LC). However, ICRA notes that a part of DTIL's creditors remain covered by bank guarantees (BGs) extended by the customers, which reduces the credit risk. Additionally, the company enters into back-to-back payment arrangement with some of its suppliers, which are either a related party to its principals or are identified by the same. This mechanism, while lowering DTIL's working capital requirements as well as credit risks, results in creation of debtor and creditor for it from the same/related parties. In the past, DTIL was able to knock-off both debtors and creditors corresponding to one of the principals when the principal got into financial trouble. Given the strong revenue growth expectations, the creditor as well as TOL are expected to increase over the medium term. In this context, ICRA takes comfort from the company's past track record of managing lean working capital cycle, its healthy liquidity position and financial flexibility.

¹ Adjusted for unencumbered liquidity

ICRA notes that the DTIL's customer concentration has reduced over the years. The strong profile of the large principals—Xiaomi Corporation [Moody's Baa2 (Stable)] and Samsung Electronics [Moody's Aa3 (Stable)]—and DTIL's position as one of the largest and cost-efficient EMS players in India, partially abates the customer concentration risk. The rating 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 high dependence on imported raw materials/components and is susceptible to any significant supply-chain disruption. In this context, ICRA notes the shortage and volatility in global supply chain of semiconductors, which is an important component of electronics products. The impact of supply chain issues on production/sales and profitability will be a key rating monitorable over the medium term. The price volatility in inputs mainly related to semiconductor, along with higher share of revenues from the mobile segment had moderated its operational profit margins (OPM) to 3.6% in FY2022 from 4.5% in FY2021. However, supported by expansion in scale of operations and increasing share of ODM business with better operating profitability, the OPM is expected to improve to 4%-4.5% over the medium term. Notwithstanding the thin operating margin due to inherent nature of business, the return indicators are likely to remain healthy in the backdrop of high asset turnover and prudent working capital management.

The Stable outlook on the rating reflects DTIL's strong business profile as one of the largest and cost-efficient EMS players in India and ICRA's expectation that it will continue to report a healthy growth in its scale of operations while improving its EBITDA margins, along with diversification in customer profile.

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. It has an established track record as well as 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 and maintain 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 consumer electronics (CE; mainly LED television), lighting, home appliances (mainly washing machines), mobiles and security devices. Further, it has presence in set-top boxes and medical electronics. While the CE, lighting, and home appliances segments are catered to by DTIL, mobile phones and medical electronics manufacturing come under its subsidiary, Padget Electronics Private Limited (PEPL; erstwhile joint venture/JV). Security devices and set-top boxes manufacturing is undertaken under another subsidiary, AIL Dixon Technologies Private Limited (JV with Aditya Infotech Limited). DTIL has recently entered/has plans to enter into decorative lightning, wearables and hearables, fully automatic washing machines, AC circuit boards, and other products. It has onboarded reputed clients under the mobile division resulting in robust growth in FY2022. The presence across multiple product segments provides DTIL a diversified revenue stream and growth opportunities. The company's clientele comprises some strong and reputed global brands such as Xiaomi, Samsung, Panasonic, Phillips, etc. The addition of new clients has supported supply chain diversification.

Robust growth in scale of operations with healthy financial risk profile – DTIL's financial profile remains healthy with robust improvement in FY2022, despite a challenging environment, supported by increased volumes in the CE and mobile vertical. The company has recorded YoY revenue growth of 66% in FY2022 (with a five-year CAGR of 34%), and ~53% in Q1 FY2023. Its revenue is expected to witness at a healthy CAGR over the medium term, supported by strong order inflows under the CE and mobile segment and addition of new segments. Further, ICRA expects the scale to grow substantially over the next few fiscals on the back of demand under the PLI scheme and ventures into new segments. The company's net worth has improved on the back of healthy accruals from operations and issuance of employee stock option programme. However, the external borrowings has increased with the ongoing capex. The credit profile remains healthy as reflected in interest coverage ratio of

7.8 times in FY2022. It plans to undertake sizeable capex, a part of which is likely to be funded by long-term borrowings, thereby increasing the debt servicing obligations. However, its increased scale and profitability is expected to keep the coverage healthy.

Credit challenges

High TOL/TNW due to high creditors and working capital requirements despite comfortable adjusted TOL/TNW ratio – DTIL has sizeable working capital requirements (both fund-based and non-fund based) due to the lead time in imports and receivables realisation period. The same gets funded, to a large extent, by the credit period from suppliers, resulting in relatively high TOL/TNW ratio and dependence on sizeable non-fund based limits (letter of credit or LC). However, ICRA notes that a part of DTIL's creditors remain covered by BGs extended by the customers, which reduces the credit risk. Additionally, the company enters into back-to-back payment arrangement with some of its suppliers, which are either a related party to its principals or are identified by the same. Adjusting for on-balance sheet liquidity, the net TOL/TNW stood at 3.3 times (as of March 31, 2022) against reported TOL/TNW of 3.6 times. Given the strong revenue growth expectations, the creditor as well as TOL are likely to increase over the medium term. Hence, its ability to raise additional long-term funds and equity remain crucial to keep the overall leverage (TOL/TNW) and current ratio manageable. DTIL's financial metrics depends on prudent management of its working capital requirements. However, ICRA takes comfort from the company's track record, its healthy liquidity position and financial flexibility.

Dependence on customers' business plans and performance – DTIL's revenues are closely linked to the business plan and performance of its principals. A major part of its revenues and operating profitability are derived from its top three customers—Xiaomi, Samsung and Panasonic. However, ICRA derives comfort from the company's long relationship with its top clients and the strong profile of the clientele. 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.

Competition and risk of technological obsolescence – The consumer durable/electronic products/EMS industry is characterised by continuous product as well as 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 the 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. Further, DTIL 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 by the company's ability to partly pass on the variation.

Liquidity position: Adequate

DTIL is likely to generate healthy cash flow from operations, supported by back-to-back arrangement with most of its suppliers for the OEM business. Its liquidity is supported by cash balance and liquid investments of Rs. 276.46 crore as on June 30, 2022 and undrawn fund-based limits – utilisation of which remained below 30% on an average over the last one year. The company proposes to undertake substantial capex in the range of Rs. 200-300 crore p.a., over the next two years, where the funding mix would comprise approx. 60% external debt and the balance through internal accruals. This is expected to increase repayment obligation, with anticipated debt repayments of Rs. 40-60 crore p.a. in FY2023 and FY2024. The fund flow from operations are estimated to remain over Rs. 300 crore p.a., adequate to meet the debt servicing obligations. Further, sufficient working capital facilities are available for meeting its working capital requirement.

Rating sensitivities

Positive factors – DTIL's ability to maintain the pace of revenue growth while achieving sustainable improvement in profitability, greater customer diversification, and improvement in its financial profile may trigger a rating upgrade. Specific credit metrics that could lead to a rating upgrade include net TOL/TNW below 2 times on a sustained basis.

Negative factors – Loss of major clients, significant slowdown in its key product segments, or supply chain disruption that materially affects its financial performance may exert negative pressure on the ratings. Additionally, inadequate long-term sources of funds for the proposed capex programme, or incremental working capital requirement, could also put pressure on its liquidity and credit profile. Increase in working capital intensity or decline in profitability resulting in weakening of liquidity and credit metrics with net TOL/TNW increasing above 3.5 or interest coverage falling below 5 times, on a sustained basis, can trigger a rating downgrade.

Analytical approach

| Analytical Approach | Comments |
|---------------------------------|---|
| Applicable rating methodologies | Corporate Credit Rating Methodology |
| Parent/Group support | Not applicable |
| Consolidation/Standalone | The ratings are based on the consolidated financial statements of the issuer, which includes its subsidiaries and JVs (refer Annexure II) |

About the company

DTIL, incorporated in 1993 by Mr. Sunil Vachani, is a diversified EMS company with operations in the electronic products vertical such as consumer electronics, lighting, home appliance, closed-circuit television cameras (CCTVs), and mobile phone. It also undertakes reverse logistics operations. It manufactures security surveillance equipment through a JV company (AIL Dixon Technologies Private Limited). Recently, the company has entered a JV with Imagine Marketing Private Limited for designing and manufacturing wireless audio solutions in India

DTIL has manufacturing facilities in Noida, Dehradun, and Tirupati. The company and its subsidiaries/JVs have received approvals under the PLI scheme for five segments - mobile phones, lightning, telecom and networking products, inverter controller boards for air conditioners and IT hardware.

The company is listed on both the National Stock Exchange (NSE) and Bombay Stock Exchange (BSE).

In FY2022, the company reported a net profit of Rs. 190.4 crore on an operating income (OI) of Rs. 10,697.1 crore against a net profit of Rs. 159.8 crore on an OI of Rs. 6,448.2 crore in the previous year.

Key financial indicators (audited)

| | FY2021 | FY2022 |
|--|---------|----------|
| Operating income | 6,448.2 | 10,697.1 |
| PAT | 159.8 | 190.4 |
| OPBDIT/OI | 4.5% | 3.6% |
| PAT/OI | 2.5% | 1.8% |
| Total outside liabilities/Tangible net worth (times) | 3.0 | 3.6 |
| Total debt/OPBDIT (times) | 0.8 | 1.9 |
| Interest coverage (times) | 8.9 | 7.8 |

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; Amount in Rs crore

Source: Company data, ICRA Research

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

| Instrument | Type | Current rating (FY2023) | | Chronology of rating history for the past 3 years | | | | | | | | | | |
|---|------------|--------------------------|---|---|-------------------------|-------------------------|-------------------|-------------------|-------------------|--------------------|-------------------------|------------------|------------------|------------------|
| | | Amount rated (Rs. crore) | Amount outstanding as on Mar 31, 2022 (Rs. crore) | Date & rating in FY2023 | Date & rating in FY2022 | Date & rating in FY2021 | | | | | Date & rating in FY2020 | | | |
| | | | | Aug 26, 2022 | Mar 29, 2022 | Mar 31, 2021 | Mar 17, 2021 | Nov 25, 2020 | Sep 28, 2020 | May 01, 2020 | Oct 11, 2019 | Oct 3, 2019 | Jun 10, 2019 | |
| 1 Commercial paper | Short Term | 175.00 | - | [ICRA]A1+ | [ICRA]A1+ | [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 | 240.0 | 179.71 | [ICRA]AA-(Stable) | [ICRA]AA-(Stable) | [ICRA]AA-(Stable) | [ICRA]AA-(Stable) | [ICRA]AA-(Stable) | [ICRA]AA-(Stable) | [ICRA]A+(Positive) | [ICRA]A+(Stable) | [ICRA]A+(Stable) | [ICRA]A+(Stable) | [ICRA]A+(Stable) |
| 3 Fund-based - Working capital facilities | Short Term | 650.0 | - | [ICRA]A1+ | [ICRA]A1+ | [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 | 1735.0 | - | [ICRA]A1+ | [ICRA]A1+ | [ICRA]A1+ | [ICRA]A1+ | [ICRA]A1+ | [ICRA]A1+ | [ICRA]A1+ | [ICRA]A1+ | [ICRA]A1+ | [ICRA]A1+ | [ICRA]A1+ |
| 6 Unallocated bank facilities | Short Term | - | - | - | [ICRA]A1+ | [ICRA]A1+ | [ICRA]A1+ | [ICRA]A1+ | [ICRA]A1+ | [ICRA]A1+ | [ICRA]A1+ | [ICRA]A1+ | [ICRA]A1+ | - |

Complexity level of the rated instruments

| Instrument | Complexity Indicator |
|---|----------------------|
| Commercial paper | Very Simple |
| Fund-based -Term loan | Simple |
| Fund-based - Working capital facilities | Simple |
| Non-fund based - Working capital facilities | Very Simple |

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: www.icra.in

Annexure I: Instrument details

| ISIN | Instrument Name | Date of Issuance | Coupon Rate | Maturity | Amount Rated (Rs. crore) | Current Rating and Outlook |
|-----------|---|------------------|-------------|----------|--------------------------|----------------------------|
| Unplaced* | Commercial paper* | NA | NA | NA | 175.00 | [ICRA]A1+ |
| NA | Fund-based - Working capital facilities | NA | NA | NA | 650.00 | [ICRA]A1+ |
| NA | Non-fund based - Working capital facilities | NA | NA | NA | 1,735.00 | [ICRA]A1+ |
| NA | Fund-based - Term loan | FY2021 | NA | FY2029 | 240.00 | [ICRA]AA- (Stable) |

*No CP was outstanding as of July 2022; ^ between non-fund based and fund based, Source: DTIL

[Please click here to view details of lender-wise facilities rated by ICRA](#)

Annexure II: List of entities considered for consolidated analysis

| Company Name | Ownership | Consolidation Approach |
|---|-----------|------------------------------------|
| Dixon Global Private Limited | 100% | Full Consolidation |
| Padget Electronics Private Limited | 100% | Full Consolidation |
| Dixon Electro Manufacturing Private Limited | 100% | Full Consolidation |
| Dixon Technologies Solutions Private Limited | 100% | Full Consolidation |
| Dixon Electro Appliances Private Limited | 51% | Full Consolidation |
| AIL Dixon Technologies Private Limited | 50% | Proportionate Consolidation Method |
| Rexxam Dixon Electronics Private Limited (Formerly known as Dixon Devices Private Limited) | 40% | Proportionate Consolidation Method |

Source: Company, ICRA Research

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