November 29, 2023

Dixon Technologies (India) Limited: Ratings reaffirmed; outlook revised to Positive from Stable

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term – Fund-based – Term loan	75.00	75.00	[ICRA]AA- reaffirmed; Outlook revised to 'Positive' from 'Stable'
Short-term – Fund-based – Working capital facilities	710.00	710.00	[ICRA]A1+; reaffirmed
Short-term – Non-fund based – Working capital facilities	1,785.00	1,785.00	[ICRA]A1+; reaffirmed
Long-term /Short-term – Unallocated	55.00	55.00	[ICRA]AA-/ [ICRA]A1+ reaffirmed; Outlook revised to 'Positive' from 'Stable'
Total	**2,625.00**	**2,625.00**	

**Instrument details are provided in Annexure-I*

Rationale

The revision in outlook to Positive reflects ICRA's expectation of a sustained improvement in Dixon Technologies (India) Limited's (DTIL) credit profile going forward, led by enhanced operating performance across its business segments in the backdrop of healthy growth in order inflow and customer diversification in the last 12-18 months. In addition, continued focus on backward integration and increase in Original Design Manufacturing (ODM) business are expected to support its profitability indicators and leverage metrics over the medium term.

The ratings continue to derive comfort from the Dixon Group's (viz. the company and its subsidiaries/joint ventures or JVs) strong operating profile, characterised by an 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, mobiles, washing machines, etc.) and well-established relationships with a reputed clientele. In the last 12-18 months, the Group has deepened its relationship with the existing players (Samsung, Xiaomi, etc) and has onboarded several new clients across segments - Transsion Group, Reliance Jio and Xiaomi (mobiles), Voltas and Bosch (home appliances), Airtel and Jio (telecom and networking products), Acer and Lenovo (IT hardware), among others. The Group is a beneficiary under the production-linked incentive (PLI) scheme for five segments – mobile phones, lightning, telecom and networking products, inverter controller boards for air conditioners and IT hardware. A part of the incentives realised, so far, have also been shared with the clients. A conducive policy environment (thrust on Make-in-India), healthy domestic demand (led by low penetration levels) and China+1 strategy of global manufacturers (diversification of supply chains) are expected to support a faster ramp-up of DTIL's scale of operations over the medium term. Accordingly, it has been investing in capacity expansion along with backward integration, which is likely to continue over the next 2-3 years.

ICRA notes the robust growth in DTIL's scale of operations at a four-year CAGR of 43%, with YoY growth of 14% in FY2023 and 22% in H1 FY2024, which imparts economies of scale benefit. Its healthy financial profile is reflected in strong return on capital employed (RoCE) and comfortable debt coverage indicators with an interest cover of 8.1 times in FY2023. The company has consistently been taking initiatives to increase the value addition (i.e., higher share of ODM business). Coupled with correction in commodity prices, these measures led to an improvement in DTIL's operating profit margins (OPM) to 4.2% in FY2023 (4% in H1 FY2024) from 3.6% in FY2022. ICRA expects a higher share of prescriptive business (especially in mobiles, IT hardware segment) will limit any material rise in its OPM from the current levels. Nonetheless, the RoCE is expected to improve due to relatively lower blockage of funds in the working capital business under prescriptive business.

DTIL has sizeable working capital requirements due to the lead time in imports and receivables realisation period. The same gets funded largely 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 for Xiaomi 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 customers 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. Adjusted for such back-to-back arrangements, company's adjusted net TOL/TNW stood at 1.5 times as on March 31, 2023 (1.8 times as on March 31, 2022). Given the strong revenue growth expectations, the creditors and consequently the total outside liabilities 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 (NWC/OI of 0-5% over the last three years; 1.3% in FY2023), its healthy liquidity position and financial flexibility. Going forward, company's ability to judiciously management working capital cycle remains crucial to maintain a comfortable liquidity position and remains a key monitorable.

The Group has dependence on a few large customers, which exposes its revenues to business plans and performance of the same. However, DTIL's customer concentration has reduced over the years. The strong profile of its largest customers — Motorola Mobility LLC, Xiaomi Corporation [Moody's Baa2 (Stable)] and Samsung Electronics [Moody's Aa2 (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. Nonetheless, the company's extensive experience in managing these diverse risks provide comfort.

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 its key segments of operations, i.e., LED television, mobiles and EMS division, lighting, and home appliances. 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 helped DTIL in adding new principals and maintain healthy relationship with its clients, resulting in repeat business. The ratings note the realisation of incentives under the mobile phone, telecom and networking products segment, along with achievement of thresholds under PLIs for white goods, i.e., LED components and AC PCBs. It has also been declared as a beneficiary under PLI 2.0 for IT hardware.

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, telecom and networking products, hearables and wearables, and security devices. While the CE, lighting, and home appliances segments are catered to by DTIL, mobile phones and IT hardware manufacturing come under its wholly-owned subsidiary, Padget Electronics Private Limited (PEPL). Security devices, wearables and hearables as well as air conditioner–printed circuit boards (AC-PCBs) manufacturing is undertaken in JVs established with Aditya Infotech Limited, Imagine Marketing Limited and Rexxam Group, respectively. DTIL has recently entered product categories like refrigerators, strip and rope lighting and commercial displays. It has onboarded reputed clients under the mobile division resulting in healthy growth in FY2023 and H1 FY2024. 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 Motorola, Xiaomi, Samsung, Itel, Airtel, Reliance Jio, Acer, Lenovo, etc. The addition of new clients has supported supply-chain diversification as well.

Robust growth in scale of operations with healthy coverage metrics and return indicators – DTIL's financial profile remains healthy with strong YoY revenue growth in FY2023 and H1 FY2024, supported by increased volumes primarily in the mobile vertical. It has recorded YoY revenue growth of 14% in FY2023 (with a four-year CAGR of ~43%), and 22% in H1 FY2024. 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, driven by healthy accruals from operations and issuance of employee stock option programme. The credit profile remains healthy as reflected in interest coverage ratio of 8.1 times in FY2023 and 10.6 times in H1 FY2024. While the Group plans to undertake sizeable capex, a part of which is likely to be funded by long-term borrowings, its increased scale and profitability are expected to keep the coverage metrics at a comfortable level.

Credit challenges

Working capital-intensive nature of business – The company faces competition from other EMS players, besides exposure to in-house manufacturing capacities of its principal customers. This 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. Going forward, the margins are expected to remain at around 4%. Further, DTIL has sizeable working capital requirements due to the lead time in imports and receivables realisation period. However, this gets funded largely by the credit period from suppliers, which results in a relatively high adjusted net TOL/TNW[1] ratio (1.5 times as on March 31, 2023 and 1.9 times as on September 30, 2023) and dependence on sizeable non-fund based limits. Given the strong revenue growth expectations, the creditor and the total outside liabilities are likely to increase over the medium term. In this context, ICRA takes comfort from the company's past track record of managing a lean working capital cycle, its healthy liquidity position and financial flexibility.

Exposed to geopolitical risks and susceptibility of revenues to performance of key customers – Given DTIL's import dependence for several key components (battery cells, other raw material for electronics), it would remain vulnerable to geo-political developments between India and RM exporting nations over the near to medium term. Any change in regulations related to imports of components or supply-chain disruptions could likely impact its operations. Further, DTIL's revenues are closely linked to the business plan and performance of its customers. 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. With ramp-up in sales to several new customers added across segments over the last 12-18 months, the customer concentration is expected to reduce sequentially over the medium term. Nevertheless, it needs to make continuous efforts to maintain its cost competitiveness and upgrade to new products, considering the dynamic nature of the product segments.

Liquidity position: Adequate

DTIL is likely to generate healthy cash flow from operations, driven by a healthy working capital cycle. Its liquidity is further supported by cash balance and liquid investments of Rs. 126.6 crore as on September 30, 2023 and undrawn fund-based limits (around Rs. 1,160 crore at a consolidated level as on September 30, 2023). The average fund-based limit utilisation had been less than 25% over the last one year. The company intends to undertake capex in the range of Rs. 300 - 400 crore p.a., over the next two years, partly funded by external debt. In addition, it is estimated to have debt repayment obligations of Rs. 90 - 110 crore p.a. in FY2025 and FY2026. Its cash flows from operations are expected to remain adequate to meet all these funding obligations. Further, sufficient cushion in the working capital facilities is available for meeting any working capital mismatch.

Environmental and social risks

Environmental considerations – Electronics manufacturing industry is an energy-intensive process requiring substantial quantities of fuel and thus, resulting in greenhouse gas emissions, waste generation and pollution. As such, the industry (and DTIL) remains exposed to litigation/penalties arising from issues related to waste and pollution management. As per the

[1] *Adjusted net TOL/TNW ratio: For arriving at adjusted net TOL/TNW, the TOL has been adjusted by netting off cash balances and liquid investments and creditors which are either covered by BGs or where clients and suppliers are covered under back-to-back arrangement.*

company's annual report of FY2023, it has been taking initiatives towards the use of sustainable technology and energy efficiency. It is continually augmenting the renewable energy contribution in the total energy mix. Nonetheless, DTIL's cash flows remain exposed to the increasing investment requirements to comply with stringent pollution norms (recycling or safe waste disposal).

Social considerations – Social risks in the industry stem from the health and safety concerns of employees involved in the manufacturing process. It also remains exposed to any major shift in consumer preferences, which are a key driver for demand, and accordingly may need to make material investments to realign its product portfolio.

Rating sensitivities

Positive factors – DTIL's ability to maintain the pace of revenue growth while achieving sustainable improvement in operating margins, greater customer diversification, and improvement in its leverage as well as coverage metrics may trigger a rating upgrade. Specific credit metrics that could lead to a rating upgrade include adjusted net TOL/TNW[2] below 1.5 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 leverage and coverage metrics may exert negative pressure on the ratings. Additionally, any asset liability mismatch or deterioration in working capital intensity, which materially impacts liquidity position will be a credit negative. Adjusted net TOL/TNW increasing above 2.25 times 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 Electronic Manufacturing Services (EMS) company with operations in the electronic products vertical such as consumer electronics, lighting, home appliance, closed-circuit television cameras (CCTVs) and mobile phones. It also undertakes reverse logistics operations. Besides, it manufactures security surveillance equipment, wearables and hearables, AC-PCBs. Recently, it has entered a JV with Imagine Marketing Private Limited for designing and manufacturing wireless audio solutions in India.

Headquartered in Gurgaon, DTIL has around 21 manufacturing facilities (at a consolidated level) across Noida (Uttar Pradesh), Dehradun (Uttarakhand), Ludhiana (Punjab), and Chittoor (Andhra Pradesh). In the last few years, the company and its subsidiaries/JVs have received approvals under the production-linked incentive (PLI) scheme for five segments - mobile phones, lightning, telecom and networking products, inverter controller boards for air conditioners and IT hardware.

[2] *Adjusted net TOL/TNW ratio: For arriving at adjusted net TOL/TNW, the TOL has been adjusted by netting off cash balances and liquid investments and creditors which are either covered by BGs or where clients and suppliers are covered under back-to-back arrangement.*

Key financial indicators (audited)

DTIL (Consolidated)	FY2022	FY2023	H1 FY2024
Operating income	10,697.1	12,192.0	8,214.7
PAT	190.4	253.5	175.1
OPBDIT/OI	3.6%	4.2%	4.0%
PAT/OI	1.8%	2.1%	2.1%
Total outside liabilities/Tangible net worth (times)	3.6	2.8	3.3
Total debt/OPBDIT (times)	2.5	1.2	0.9
Interest coverage (times)	7.8	8.1	10.6

Source: Company data, ICRA Research; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; Amount in Rs. crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

		Current Rating (FY2024)						Chronology of Rating History for the past 3 years						
SN	Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding as on Aug 31, 2023 (Rs. crore)	Date & Rating in			Date & Rating in FY2023	Date & Rating in FY2022	Date & Rating in FY2021				
					Nov 29, 2023	Aug 30, 2023	Apr 06, 2023	Aug 26, 2022	Mar 29, 2022	Mar 31, 2021	Mar 17, 2021	Nov 25, 2020	Sep 28, 2020	May 01, 2020
1	Commercial paper	Short Term	-	-		[ICRA]A1+; withdrawn	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
2	Fund-based - Term loan	Long Term	75.00	68.3	[ICRA]AA-(Positive)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]A+(Positive)	[ICRA]A+(Stable)
3	Fund-based - Working capital facilities	Short Term	710.00	-	[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	1,785.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
5	Unallocated bank facilities	Long term/ Short Term	55.00	-	[ICRA]AA-(Positive)/ [ICRA]A1+	[ICRA]AA-(Stable)/ [ICRA]A1+	[ICRA]AA-(Stable)/ [ICRA]A1+	-	-	-	-	-	-	-

6	Unallocated bank facilities	Short Term	-	-	-	-	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

Complexity level of the rated instruments

Instrument	Complexity Indicator
Fund-based – Term loan	Simple
Fund-based – Working capital facilities	Simple
Non-fund based – Working capital facilities	Very Simple
Unallocated bank facilities	Not Applicable

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: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	**Fund-based – Working capital facilities**	NA	NA	NA	710.00	[ICRA]A1+
NA	**Non-fund based – Working capital facilities**	NA	NA	NA	1,785.00	[ICRA]A1+
NA	**Fund-based – Term loan**	FY2021	NA	FY2029	75.00	[ICRA]AA- (Positive)
NA	**Unallocated bank facilities**	NA	NA	NA	55.00	[ICRA]AA-(Positive) /[ICRA]A1+

Source: DTIL, ICRA Research

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 Pvt. Ltd.	100%	Full Consolidation
Dixon Electro Manufacturing Private Limited	100%	Full Consolidation
Dixon Technologies Solutions Private Limited	100%	Full Consolidation
Dixtel Communications Private Limited	100%	Full Consolidation
Dixon Electro Appliances Private Limited	51%	Full Consolidation
AIL Dixon Technologies Private Limited	50%	Equity Method
Califonix Tech and Manufacturing Private Limited	50%	Equity Method
Rexxam Dixon Electronics Private Limited (formerly known as Dixon Devices Private Limited)	40%	Equity Method

Source: Company, ICRA Research

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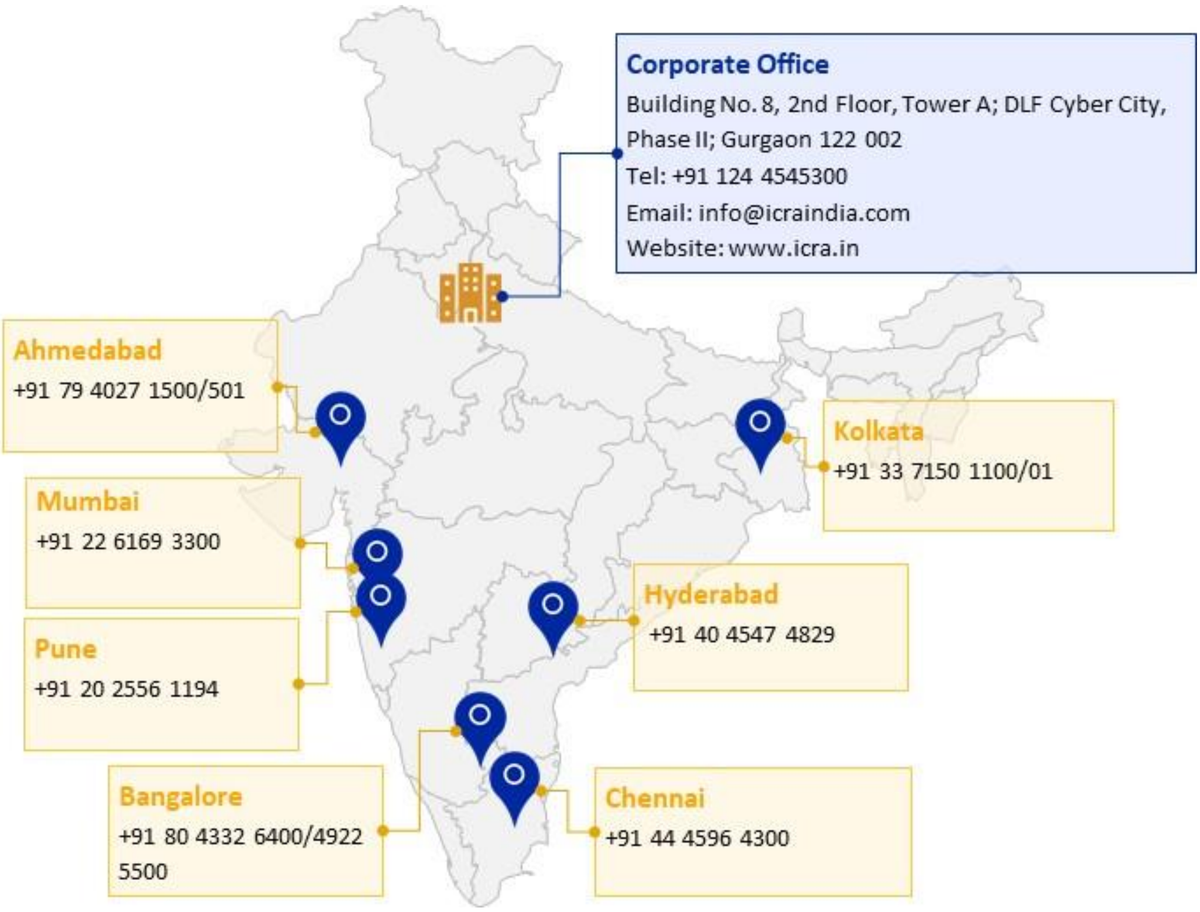

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