

May 01, 2020

Dixon Technologies (India) Limited (erstwhile Dixon Technologies (India) Private Limited): [ICRA]A1+ assigned for enhanced amount

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Commercial Paper	50.00	100.00	[ICRA]A1+; Assigned/ Outstanding
Fund-based -Term Loan	4.70	4.70	[ICRA]A+ (Stable); Outstanding
Fund-based - Working Capital Facilities	95.00	95.00	[ICRA]A1+; Outstanding
Non-fund Based - Working Capital Facilities (Short term scale)	635.00	635.00	[ICRA]A1+; Outstanding
Interchangeable^ Working Capital Facilities (Short term scale)	250.00	250.00	[ICRA]A1+; Outstanding
Unallocated Bank facilities (Short term scale)	45.30	45.30	[ICRA]A1+; Outstanding
Total	1080.00	1130.00	

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

Rationale

The ratings take into account the healthy operating profile of Dixon Technologies (India) Limited (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, and washing machines) 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 improvement in profitability 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 their business plans and performance. The revenue concentration, though reduced over the years, remains due to the high dependence on a few clients. However, the strong profile of the large principals, 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. This apart, 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, though the same gets funded to an extent by the credit period from suppliers. However, due to sizeable creditors, the dependence on non-fund based limits (letter of credit or LC) remains high. With the Covid-19 related disruption, and sizeable LC exposure, the company will be dependent on timely realisation of receivables, or an extension of credit period from suppliers, and LC maturity, without which the liquidity position could be impacted and dependence on borrowing could increase in the near term. Further, the Covid-19 related lockdown has resulted in shutdown of DTIL's plants and has also disrupted its supply chain as a significant part of its raw material is imported from China. ICRA expects a gradual and staggered resumption of manufacturing activities after the lockdown is lifted. The overall slowdown in economy is expected to result in

curtailment of discretionary expenditure, thereby impacting the demand for white goods and consumer durables as well. As the Covid-19 situation is still evolving, an extended lockdown/shutdown of production/supply disruption, or demand contraction could create pressure on the credit profile of DTIL and therefore would be a key monitorable. However, ICRA takes comfort from the company's current healthy liquidity position and financial flexibility.

Key rating drivers and their description

Credit strengths

Established track record and market position in EMS business; established clientele: DTIL has more than two decades of experience in the EMS business and has established a track record and a 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.

Reputed clientele and diversified revenue streams across product segments: DTIL's clientele comprises some strong and reputed global brands like Phillips, Panasonic, Xiaomi, etc. The company's revenues are also diversified across product segments like consumer electronics (CE, mainly LED television), lighting, home appliances (mainly washing machines), mobiles, and security devices. While the CE, lighting, and home appliances segments are catered to by DTIL, the mobile phones and security devices manufacturing come under its subsidiary Padget Electronics Private Limited (erstwhile JV) and 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.

Healthy financial profile with moderate leverage and healthy debt coverage metrics: DTIL's has a healthy financial profile with strong revenue growth in 9M FY2020 supported by increased volumes in 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 ESOP programme in 9M FY2020, while external borrowing has remained limited and primarily comprises working capital borrowings. The credit profile remained healthy as reflected in interest coverage ratio of 6.2 times and debt service coverage ratio of 4.3 times in 9M FY2020. DTIL's credit profile is expected to remain healthy, though the current Covid-19 related disruption would result in some moderation in its financial performance in the near term. Nevertheless, as the Covid-19 situation is evolving, an extended lockdown/shutdown of production, or demand contraction could create pressure on the credit profile of DTIL and therefore would be a key monitorable.

Credit challenges

Dependence on customers' business plans and performance; however, strong patronage of its 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 – Philips, Panasonic, and Xiaomi. However, ICRA derives comfort from the company's long relationship with two of the top three clients (Phillips – over 13 years; Panasonic – over five years) and their strong patronage. 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 the 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, which limits 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.

Working capital requirements: DTIL's operations require sizeable working capital limits (fund based and non-fund based). The company imports over 40% of its raw material requirements. A sizable portion of these imports are backed by usance LCs. Typically, the usance period covers the cash conversion cycle, i.e. lead time in imports and receivables, production and realisation period. Therefore, at any given point in time, the company has a sizable utilisation of NFB limits. Further, it utilises fund-based facilities like bill discounting and other working capital borrowings to meet its other working capital requirements. With the Covid-19 related disruption, and sizeable LC exposure, the company will be dependent on timely realisation of receivables, or an extension of credit period from suppliers, and LC maturity, without which the liquidity position could be impacted and dependence on borrowing could increase in the near term.

Challenges associated with Covid-19: The Covid-19 related lockdown has resulted in shutdown of DTIL's plants in three locations — Noida (Uttar Pradesh), Dehradun (Uttarakhand), and Tirupati (Andhra Pradesh). The management expects the Dehradun plant to resume operations shortly, with appropriate measures like social distancing and healthy monitoring of workers. However, labour availability may be an issue on account of migration of labour workforce during the lockdown. Further, the slowdown in economic activity due to lockdown may impact the discretionary spending of consumers and affect demand for electronic goods and consequently, volumes for Dixon. Therefore, ICRA expects a gradual and staggered resumption of manufacturing activities after the lockdown is lifted. Hence, the operational and financial performance of the company is expected to be moderated in the near term.

ICRA takes comfort from healthy liquidity position and financial flexibility of the company. However, as the Covid-19 situation is still evolving, an extended lockdown/shutdown of production, or demand contraction could create pressure on the credit profile of DTIL and therefore, would be a key monitorable.

Liquidity position: Adequate

The company had cash and bank balance of Rs. 104.71 at the end of March 2020 and cushion in working capital limits (fund-based limit utilisation was low in the recent past). While the sizeable letter of credit (LC) exposes DTIL to risk of cash flow mismatch due to the Covid-19 related disruption, ICRA has taken into considerations the available cushion in fund-based working capital limits, and steps taken by the company to extend LC maturity. Nevertheless, this would remain a key monitorable in the near term and can impact liquidity.

Rating sensitivities

Positive triggers – ICRA could upgrade DTIL's rating if the company maintains its pace of revenue growth while achieving sustainable improvement in profitability and greater customer diversification and improvement in financial profile. Specific credit metrics that could lead to an upgrade of Dixon's rating include (1) Total Outside Liabilities (TOL)/Tangible Net Worth (TNW) below 2.0 times.

Negative triggers – Negative pressure on DTIL's rating could arise if the loss of any large client or slowdown in its key product segments materially affects its financial performance. The ratings could be downgraded if any increase in

working capital intensity results in tightening of liquidity position or stretching payables results in an increase in leverage to TOL/TNW of over 3.0 times on a sustained basis. The rating may also be downgraded if the Covid-19 related disruption prolongs and results in demand contraction or considerably weakens its liquidity position.

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 player with operations in various subsegments of the electronics vertical. DTIL has operations in consumer electronics, lighting, home appliance, and mobile phone segments and also undertakes reverse logistics operations. Besides, the company also undertakes manufacturing of mobiles and security surveillance equipment in subsidiaries/JVs.

TV manufacturing, part of CE vertical, has been the largest segment for DTIL, over the years. The company has recently added Xiaomi as a customer for 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 and backward integration in the lighting segment has supported profitability improvements in the recent years. DTIL ventured into mobiles manufacturing in 2016 through its 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 became its wholly owned subsidiary. The company has recently started manufacturing feature phones under the standalone venture. 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. In September 2017, the company came out with an IPO worth ~Rs. 600 crore, which involved ~Rs. 60 crore of fresh equity issuance and remaining as offer for sale from promoter/investors.

In FY2019, the company reported a net profit of Rs. 63.4 crore on an operating income (OI) of Rs. 2,984.4 crore compared to a net profit of Rs. 60.9 crore on an OI of Rs. 2,841.6 crore in the previous year. In 9M FY2020, it reported net profit of Rs. 92.9 crore on an OI of Rs. 3,542.6 crore.

Key financial indicators (audited)

	FY2018	FY2019	9mFY2020
Operating Income (Rs. crore)	2,841.6	2,984.4	3542.7
PAT (Rs. crore)	60.9	63.4	92.9
OPBDIT/OI (%)	4.0%	4.6%	4.8%
RoCE (%)	30.4%	23.2%	-
Total Outside Liabilities/Tangible Net Worth (times)	2.4	3.2	-
Total Debt/OPBDIT (times)	1.2	1.8	-
Interest Coverage (times)	8.0	5.2	6.2*
DSCR	5.2	3.8	-

* The ratio excluding interest on lease obligation is 7.1 times

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Instrument	Rating (FY2021)				Current Rating 01-May-2020	Rating History for the Past 3 Years					
	Type	Amount Rated	Amount Outstanding	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	25.00	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
2 Fund-based -Term Loan	Long Term	4.70	4.70	[ICRA]A+ (Stable)	[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	95.00	-	[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+
5 Interchangeable^ Working Capital Facilities	Short Term	250.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	-
6 Unallocated Bank facilities	Short Term	45.30	-	[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	18-Nov-2015	NA	30-Sep-2020	4.70	[ICRA]A+ (Stable)
NA	Fund-based - Working Capital Facilities	NA	NA	NA	95.00	[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	45.30	[ICRA]A1+

*CP programme to the extent of Rs. 25 crore has been placed as of April 30, 2020; ^ 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	*50.00%	Proportionate Consolidation Method/ Equity Method
AIL Dixon Technologies Private Limited	50.00%	Proportionate Consolidation Method/ Equity Method

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

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