ICRA

September 28, 2020

Dixon Technologies (India) Limited (erstwhile Dixon Technologies (India) Private Limited): Ratings reaffirmed, outlook on long-term rating revised to Positive; rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based -Term Loan	4.70	52.70	[ICRA]A+ (Positive); Reaffirmed, outlook revised from 'Stable' to 'Positive'
Fund-based - Working Capital Facilities	95.00	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)	45.30	47.34	[ICRA]A1+; Reaffirmed
Commercial Paper	100.00	100.00	[ICRA]A1+; Reaffirmed
Total	**1130.00**	**1230.04**	

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

Rationale

The revision in outlook to Positive takes into account the scaling up of Dixon Technologies (India) Limited's (DTIL) operating income (OI) as well as improvement in its profitability and working capital position over the past year. Despite the disruption in operations due to the Covid-19 pandemic-related lockdown, the performance of DTIL has remained satisfactory in Q1 FY2021 and it has witnessed strong recovery in business post easing of Covid-19-related curbs. The Positive outlook on the long-term rating stems from ICRA's expectation that DTIL would continue to scale up its operations and profits along with increasing client and product diversification. The scale-up could be significant if the company's application for Production Linked Incentive (PLI) scheme is approved. This is expected to help the company in sustaining and further improving its credit metrics over the medium term.

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 a 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 the business plans and performance of the same. The revenue concentration, though reduced over the years, remains due to the company's 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. The financial metrics of DTIL, therefore, 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. ICRA positively takes into account the improvement in total outside liabilities/tangible net worth (TOL/TNW) from 3.2x as of March 31, 2019 to 2.3x as of March 31, 2020 (net TOL/TNW adjusted for cash and liquid investments stood at 2.1x as of March 31, 2020).

While reaffirming the rating, ICRA has noted the uncertain Covid-19 pandemic situation that could impact corporates including DTIL in short term. Any re-imposition of localised lockdown/shutdown of production/supply disruption to contain the pandemic could impact its operating performance and will remain a sensitivity. Further DTIL, like other electronics manufacturers, has a high dependence on imported raw materials/components. Any significant supply-chain disruption could create pressure on the credit profile of DTIL and therefore, would be a key monitorable.

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 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.

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. 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. DTIL's clientele comprise some strong and reputed global brands like Xiaomi, Panasonic, Phillips, etc.

Healthy financial profile with moderate leverage and healthy debt coverage metrics: DTIL's financial profile remained healthy with strong revenue growth in FY2020, 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 in 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 5.8 times and debt service coverage ratio of 4.3 times in FY2020. The liquidity position remains comfortable with adequate cushion in fund-based working capital limits. While the nationwide lockdown and labour/logistic challenges have impacted its performance in Q1 FY2021, it has remained healthy supported by a robust recovery since June 2020. Further, DTIL and its subsidiary have made applications for manufacturing mobile phones under the Ministry of Electronics and Information Technology (MEIT)'s PLI scheme for large scale electronics manufacturing. This could provide significant boost to DTIL's scale of operations and its profits, given the incentive available under the scheme. The company has plans to undertake debt-funded capex to would increase its long-term borrowings; however, its coverage profile is expected to remain comfortable.

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, Panasonic and Signify (previously Philips Lighting). However, ICRA derives comfort from the company's long relationship with two of the top three clients (Signify/Philips – over 13 years; Panasonic – over 5 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: DTIL's business calls for sizeable dependence on supplier's credit, though most of these have back-to-back arrangements with clients, resulting in high TOL/TNW. Nonetheless, the metric has improved from 3.2x as of March 31, 2019 to 2.3x as of March 31, 2020 (net TOL/TNW adjusted for cash and liquid investments stood at 2.1x as of March 31, 2020). The company's operations also 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 letters of credit (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 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 cyclicality in working capital requirement, given the high sales of electronic products near festive season. Therefore, the financial metrics of DTIL remain critically dependant on prudent management of its working capital requirements. In this context, ICRA takes comfort from the company's track record, and its healthy liquidity position and financial flexibility.

Impact of Covid-19 pandemic and high import dependence: ICRA has noted the uncertain Covid-19 pandemic situation, and tensions with China which could impact DTIL's credit profile. The Covid-19 pandemic risk remains and hence, any re-imposition of localised lockdown/shutdown of production/supply disruption could affect its operating performance. Further DTIL, like other electronics manufacturers, has a high dependence on imported raw materials/components. Any significant supply chain disruption/elongation could create pressure on the credit profile of DTIL and therefore, would be a key monitorable.

Liquidity position: Adequate

DTIL has **adequate** liquidity, as reflected in the free cash balance of Rs. 95.7 crore as on March 31, 2020. Further, the company's fund-based limit utilisation has remained moderate and it has undrawn fund-based limits of Rs. 92 crore as on June 30, 2020. DTIL has healthy cash generation from operation, which supports its liquidity position. The liquidity position is expected to remain adequate with the healthy cash generation and limited scheduled repayment.

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. Greater customer diversification and improvement in financial profile will be the other positive triggers. Specific credit metrics that could lead to an upgrade of DTIL's rating include TOL/TNW below 2.0 times on a sustainable basis.

Negative triggers – The outlook on ratings could be revised to Stable from Positive if the loss of any large client or slowdown in its key product segments materially affects its financial performance. The outlook could also be revised if any increase in working capital intensity or decline in profitability results in tightening of the liquidity position or stretching payables results in an increase in leverage to TOL/TNW of over 2.5 times on a sustained basis. The rating may also be downgraded in case of supply chain disruption materially affecting the company's financial performance.

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 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, 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. 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.

Key financial indicators (audited)

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

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Rating (FY2021) Type	Amount Rated	Amount Outstanding As on 30-Jun-20	Current Rating 28-Sep-2020	Earlier Rating 01-May-2020	Rating History for the Past 3 Years FY2020 11-Oct-2019	3-Oct-2019	10-Jun-2019	FY2019 1-Mar-2019	20-Sep-2018	FY2018 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+
2	Fund-based -Term Loan	Long Term	52.70	14.20	[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+
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	47.34	-	[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 click here

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]A+ (Positive)
NA	Fund-based -Term Loan 2	20-Jan-2020	NA	31-Jan-2026	50.00	[ICRA]A+ (Positive)
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*

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