

BUY

TP: Rs 5,200 | ▲ 21%

DIXON TECHNOLOGIES

Consumer Durables

21 October 2022

Buoyant numbers, bright prospects

- **Strong Q2 beat with topline up 38% YoY to Rs 39bn and PAT 15% ahead of our estimates at Rs 777mn**
- **EBITDA margin up 25bps QoQ to 3.8% on higher contribution from ODM verticals of lighting and home appliances**
- **Well placed to capture growing opportunities; we raise FY23/FY24 EPS 2%/5% and roll to a revised TP of Rs 5,200 (vs. Rs 4,500) – retain BUY**

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Strong Q2: Dixon posted an above-expected Q2FY23 performance as revenue grew 38% YoY to Rs 39bn (8% ahead of our estimates), led by broad-based growth across verticals (except security systems). EBITDA margin improved sequentially by 25bps to 3.8% (-17bps YoY), marginally above our 3.7% forecast. Adj. PAT came in at Rs 777mn, up 24% YoY and 15% ahead of our estimate.

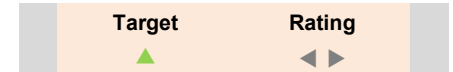
Margin aided by ODM-led verticals: The lighting & home appliance verticals generate higher margins on account of their original design manufacturing (ODM) characteristics, and performed relatively well in Q2. EBIT margin stood at 8.2% in lighting (+100bps QoQ, +20bps YoY) and 9% in home appliances (+90bps YoY, +50bps QoQ). Amongst other verticals, consumer electronics posted improvement of 20bps QoQ (+50bps YoY) to 2.9% while the mobile segment recorded a modest 2.7% margin.

Guidance maintained: Management retained its FY23 revenue guidance of Rs 150bn but remains optimistic about securing newer, larger client deals in the near future, thus offering scope for guidance revision.

Expanding ODM capabilities: Dixon is focused on expanding its ODM capabilities as it looks to capture a considerable share of India's electronic manufacturing services (EMS) industry. The joint design manufacturing (JDM) business with an anchor client has yielded desired results and the company is in active talks with other customers for additional business. It has already entered into an agreement with Google for ODM sublicensing rights relating to Android. Additionally, Dixon is setting up an injection moulding plant by Q4FY23 to deepen its network and establish backward integration.

Bright prospects; maintain BUY: Over the years, Dixon has scaled up and fortified its leadership in the EMS business. Rapid yet judicious capacity expansion on the back of strong demand, backward integration, steady client acquisition, and favourable PLI schemes are fueling a high growth trajectory. Additionally, entry into newer verticals/products and incremental ODM contribution auger well for the company. We raise FY23/FY24 EPS estimates 2%/5% and roll over to Sep'24E valuations, yielding a revised TP of Rs 5,200 (vs. Rs 4,500), set at 55x P/E, a 20% premium to the 4Y avg.

Key changes



Ticker/Price	DIXON IN/Rs 4,296
Market cap	US\$ 3.1bn
Free float	66%
3M ADV	US\$ 15.4mn
52wk high/low	Rs 5,859/Rs 3,181
Promoter/FPI/DII	34%/15%/8%

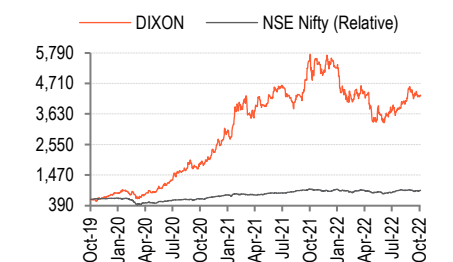
Source: NSE | Price as of 20 Oct 2022

Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	106,971	171,280	220,502
EBITDA (Rs mn)	3,791	6,625	8,841
Adj. net profit (Rs mn)	1,903	3,556	5,044
Adj. EPS (Rs)	32.1	59.9	85.0
Consensus EPS (Rs)	32.1	62.7	92.0
Adj. ROAE (%)	22.0	30.4	31.8
Adj. P/E (x)	133.9	71.7	50.5
EV/EBITDA (x)	67.2	38.5	28.8
Adj. EPS growth (%)	19.1	86.8	41.9

Source: Company, Bloomberg, BOBCAPS Research

Stock performance

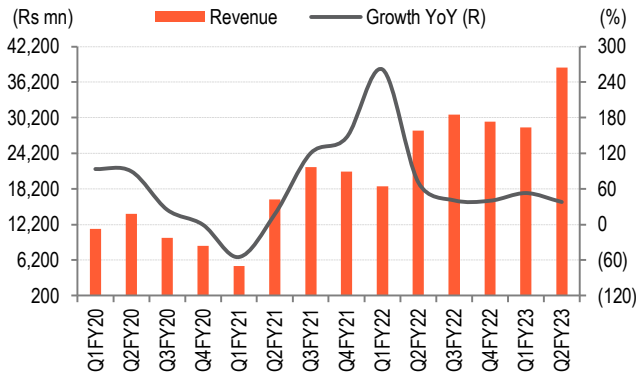


Source: NSE



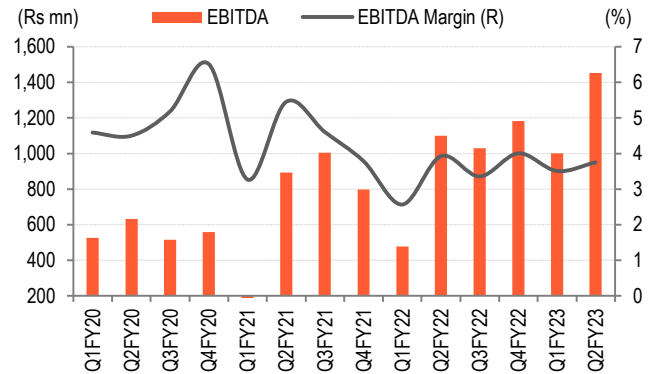
Quarterly trends

Fig 1 – Buoyant revenue growth



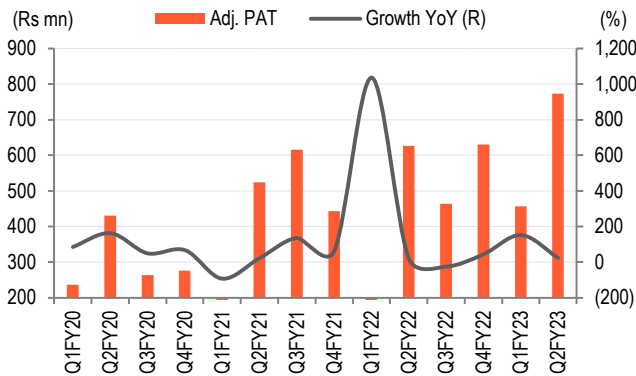
Source: Company, BOBCAPS Research

Fig 2 – Healthy margin profile



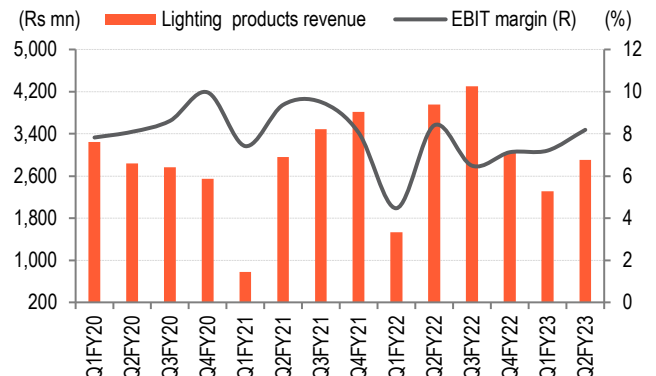
Source: Company, BOBCAPS Research

Fig 3 – Higher PAT levels



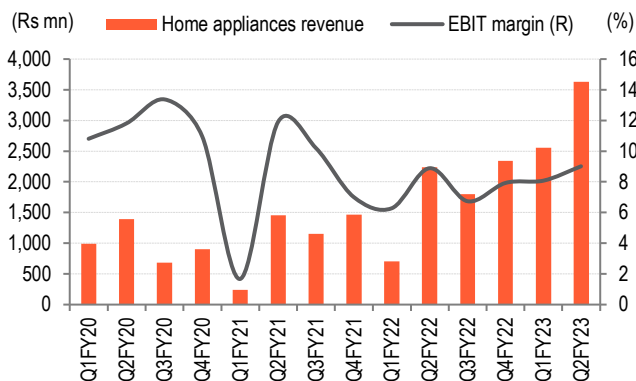
Source: Company, BOBCAPS Research

Fig 4 – Improvement in lighting product margins



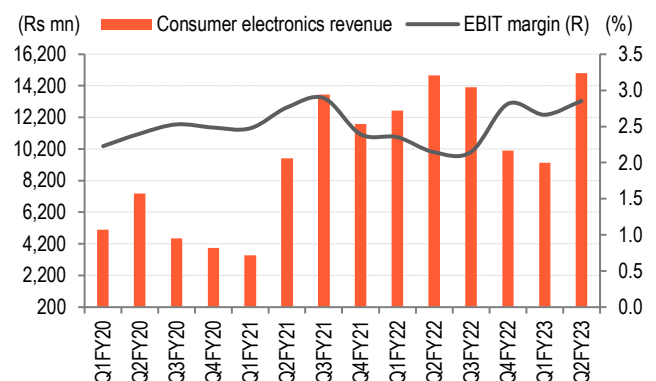
Source: Company, BOBCAPS Research

Fig 5 – Home appliances deliver strong margins



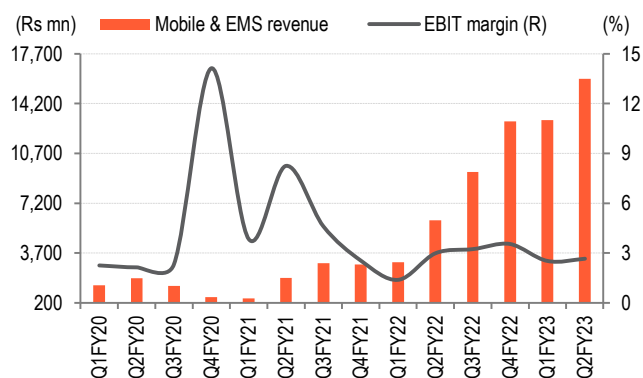
Source: Company, BOBCAPS Research

Fig 6 – Strong revenue in consumer electronics



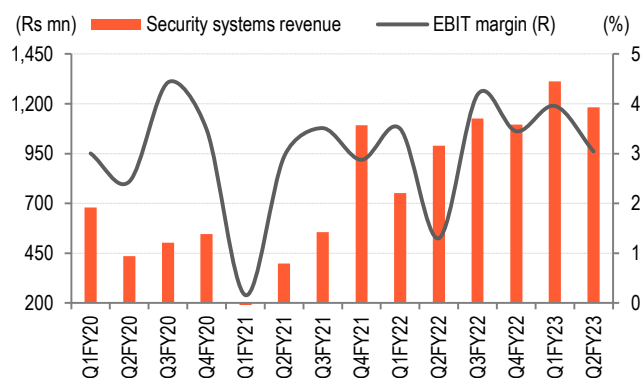
Source: Company, BOBCAPS Research

Fig 7 – Robust growth in mobile segment/EMS



Source: Company, BOBCAPS Research

Fig 8 – Security systems lagged



Source: Company, BOBCAPS Research

Fig 9 – Quarterly performance

(Rs mn)	Q2FY23	Q2FY22	YoY (%)	Q1FY23	QoQ (%)
Revenue	38,668	28,038	37.9	28,551	35.4
EBITDA	1,452	1,100	32.0	1,001	45.0
EBITDA margin (%)	3.8	3.9	(17bps)	3.5	25bps
Depreciation	291	216	-	241	-
Interest	158	91	-	144	-
Other Income	6	10	-	4	-
PBT	1,008	802	25.6	621	62.4
Tax	231	176	-	165	-
Adjusted PAT	777	626	24.0	455	70.7
Exceptional item	-	-	-	0	-
Reported PAT	772	626	23.3	457	69.0
Adj. PAT margin (%)	2.0	2.2	(22bps)	1.6	54bps
EPS (Rs)	13.1	10.6	24.0	7.7	70.7

Source: Company, BOBCAPS Research

Fig 10 – Actual vs. Estimates

(Rs mn)	Actual	Estimate	Variance (%)
Revenue	38,668	35,798	8.0
EBITDA	1,452	1,323	9.7
EBITDA margin (%)	3.8	3.7	10bps
Adj. PAT	777	673	15.4

Source: Company, BOBCAPS Research

Fig 11 – Segmental performance

Particulars (Rs mn)	Q1FY20	Q2FY20	Q3FY20	Q4FY20	Q1FY21	Q2FY21	Q3FY21	Q4FY21	Q1FY22	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23
Revenue														
Consumer electronics	5,098	7,382	4,543	3,930	3,487	9,605	13,643	11,786	12,623	14,865	14,104	10,104	9,322	15,007
Lighting products	3,243	2,839	2,767	2,548	777	2,957	3,486	3,817	1,535	3,957	4,304	3,046	2,312	2,904
Home appliances	988	1,391	684	900	241	1,454	1,152	1,465	706	2,240	1,801	2,341	2,556	3,629
Mobile & EMS	1,437	1,934	1,395	603	531	1,974	2,992	2,899	3,059	5,986	9,397	12,941	13,049	15,944
Security systems	679	435	503	546	134	397	555	1,092	751	990	1,127	1,096	1,311	1,183
EBIT														
Consumer electronics	114	177	115	98	86	265	394	282	297	318	303	284	248	428
EBIT margin (%)	2.2	2.4	2.5	2.5	2.5	2.8	2.9	2.4	2.4	2.1	2.1	2.8	2.7	2.9
Lighting products	254	230	239	254	58	277	332	307	69	333	280	217	167	238
EBIT margin (%)	7.8	8.1	8.6	10.0	7.4	9.4	9.5	8.1	4.5	8.4	6.5	7.1	7.2	8.2
Home appliances	107	164	92	99	4	173	118	103	44	199	121	186	207	327
EBIT margin (%)	10.8	11.8	13.4	11.0	1.7	11.9	10.2	7.0	6.3	8.9	6.7	7.9	8.1	9.0
Mobile & EMS	32	41	32	85	20	163	138	74	42	179	303	457	328	423
EBIT margin (%)	2.2	2.1	2.3	14.1	3.8	8.2	4.6	2.5	1.4	3.0	3.2	3.5	2.5	2.7
Security systems	20	11	22	19	0	12	20	31	26	13	47	38	52	36
EBIT margin (%)	3.0	2.4	4.4	3.5	0.1	2.9	3.5	2.9	3.5	1.3	4.2	3.4	4.0	3.0

Source: Company, BOBCAPS Research

Earnings call highlights

- Management has maintained its earlier revenue guidance of Rs 150bn for FY23 with EBITDA margin in the range of 3.8-4%. The company has also guided for ROCE of 40%+ in the next two years. This may be revised upward due to the anticipated addition of a new customer; however, more clarity will emerge within a month.
- For H1FY23, the company has booked Rs 45mn as a mobile production-linked incentive (PLI).
- Regulatory developments are undoubtedly concerning, particularly with respect to restrictions on Chinese players. The Xiaomi management has assured Dixon that there will be no impact on India business, including no payment or stock lift.
- Per management, issues in the lighting industry are subsiding and internal execution challenges are being addressed, as evidenced by margins. Dixon has gained new customers via an expanded product portfolio. Further, working capital intensity has reduced by Rs 850mn in Q2FY23. According to management, it will take a quarter or more to return to normalcy.

Consumer electronics

- The ODM-JDM business has boosted margins, with volumes increased up by 54% YoY, but revenue remained flat due to a significant drop in open cell prices in the international market. We note that Dixon has the largest LED capacity in India, with 6mn catering to 35-38% of Indian demand.
- Dixon has acquired sublicense rights for Android and Google TV, which could lead to a slew of new opportunities given that Android accounts for 65% of the Indian market. The first rollout is scheduled for Q1FY24.
- To further expand its presence, the company is investing in an injection moulding facility for backward integration, which is expected to become operational by Q4FY23.
- Dell has placed an order for monitors (production has begun), with expected volumes of 0.2mn in this category.

Lighting products

- Margin expansion was aided by demand normalisation caused by channel inventory liquidation and input price moderation.
- The company is currently executing its first supply run to the UAE in Q3FY23 and is also working on a large request for quotation (RFQ) for an anchor customer in the US market.
- Dixon is in the process of acquiring a smart lighting company, with the deal expected to close in the current quarter.

Home Appliances

- Margins in home appliances have improved as a result of commodity cost pass-through, improved operational leverage, and cost-cutting measures.
- Management expects to sell 1.7-1.8mn washing machines in FY23 (1.1mn in FY22), with semiautomatics contributing 1.5mn units and Fully Automatic Top Load [FATL] contributing 200k. FATL is guided to rise to 450k in FY24 with semiautomatics growing at 8%YoY, implying 2.2mn in volumes.
- In September, Dixon achieved its highest-ever output of 160,000 semiautomatic washing machines.
- The company indicated that it is in the end stages of winning a large contract from a Japanese player for both domestic and global markets.

Mobile & EMS division

- In Q2FY23, Motorola recorded volumes of 1mn units.
- Dixon stated that it is close to bagging a large order with a couple of brands in both the domestic and export markets. Production for these brands will begin in Q4FY23.

Security & Surveillance

- Airtel's shift from imports to domestic manufacturing bodes well for the telecom business. Dixon has begun commercial production of orthomode transducer (OMT) for Airtel. It has received a large order for setup boxes, with mass production to begin in Q2FY24.
- In addition to Acer laptops, the company recently received an order for the production of 300k Lenovo tablets per year.
- Dixon's joint venture with Rexxam to produce inverter controller boards for air conditioners is now up and running. An investment of Rs 510mn over the next five years is envisaged, with Dixon's share at Rs 200mn.

Wearable & hearables

- The joint venture with Boat has reached a milestone of producing 1mn devices per month. Dixon intends to begin producing neck bands and modern watches soon.
- The company has established a dedicated plant for TWS smart watches for Samsung in Noida.

Fig 12 – Q2FY23 volumes

Products	Volumes	Products	Volumes	Products	Volumes
LED TV	1.16mn	Semiautomatic washing machine	0.46mn	Smartphone - Samsung	2.6mn
Bulb	43mn	Fully automatic washing machine	65k	Feature phone - Samsung	3.3mn
Batten	4mn	Smartphone (excl. Samsung)	1mn	CCTV	1.4mn
Downlight	1.4mn	Feature phone (excl. Samsung)	1.3mn	DVR	0.3mn
Boat	2.3mn	Telecom (OMT & modem)	100k per month		

Source: Company, BOBCAPS Research

Valuation methodology

Over the years, Dixon has scaled up and fortified its leadership in the EMS business. Rapid yet judicious capacity expansion on the back of strong demand, backward integration, steady client acquisition, and favorable PLI schemes are fueling a high growth trajectory. Additionally, entry into newer verticals/products and incremental ODM contribution auger well for the company.

We raise our FY23/FY24 EPS estimates by 2%/5% to bake in the strong Q2FY23 performance and roll over to Sep'24E valuations, yielding a revised TP of Rs 5,200 (vs. Rs 4,500). We retain our target P/E multiple at 55x, a 20% premium to the stock's four-year average, and reiterate our BUY rating.

Fig 13 – Revised estimates

(Rs mn)	New		Old		Change (%)	
	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
Sales	171,280	220,502	171,070	220,356	0.1	0.1
EBITDA	6,625	8,841	6,418	8,430	3.2	4.9
PAT	3,556	5,044	3,487	4,801	2.0	5.1
EPS (Rs)	59.9	85.0	58.8	80.9	2.0	5.1
EBITDA margin (%)	3.9	4.0	3.8	3.8	10bps	20bps

Source: Company, BOBCAPS Research

Key risks

Key downside risks to our estimates are:

- rising competition in the industry,
- inability to scale capacities, and
- inability to meet PLI targets,

Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Amber Enterprises	AMBER IN	0.9	2,199	2,300	HOLD
Blue Star	BLSTR IN	1.4	1,204	1,100	HOLD
Crompton Greaves	CROMPTON IN	2.9	381	500	BUY
Dixon Technologies	DIXON IN	3.1	4,296	5,200	BUY
Havells India	HAVL IN	9.2	1,210	1,500	BUY
Orient Electric	ORIENTEL IN	0.7	269	310	HOLD
Polycab India	POLYCAB IN	4.8	2,649	3,300	BUY
V-Guard Industries	VGRD IN	1.3	253	250	HOLD
Voltas	VOLT IN	3.5	869	1,100	HOLD

Source: BOBCAPS Research, NSE | Price as of 20 Oct 2022

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Total revenue	64,482	106,971	171,280	220,502	263,130
EBITDA	2,866	3,791	6,625	8,841	10,640
Depreciation	437	840	1,431	1,592	1,843
EBIT	2,429	2,952	5,194	7,250	8,797
Net interest inc./(exp.)	(274)	(442)	(482)	(552)	(613)
Other inc./(exp.)	16	38	42	46	51
Exceptional items	0	0	0	0	0
EBT	2,170	2,548	4,754	6,744	8,235
Income taxes	572	644	1,198	1,699	2,075
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
Reported net profit	1,598	1,903	3,556	5,044	6,160
Adjustments	0	0	0	0	0
Adjusted net profit	1,598	1,903	3,556	5,044	6,160

Balance Sheet

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Accounts payables	17,097	23,137	37,072	47,725	56,952
Other current liabilities	898	2,615	4,187	5,390	6,432
Provisions	0	0	0	0	0
Debt funds	1,513	4,580	5,073	5,812	6,452
Other liabilities	1,576	2,472	3,955	5,089	6,072
Equity capital	117	119	119	119	119
Reserves & surplus	7,256	9,849	13,286	18,212	24,253
Shareholders' fund	7,373	9,968	13,405	18,331	24,371
Total liab. and equities	28,457	42,772	63,690	82,347	100,279
Cash and cash eq.	1,641	3,174	3,241	8,103	12,576
Accounts receivables	10,891	13,564	23,463	29,082	35,375
Inventories	7,432	11,557	18,770	23,994	28,734
Other current assets	1,946	3,176	5,085	6,547	7,812
Investments	0	0	0	0	0
Net fixed assets	5,403	9,542	10,611	11,519	12,176
CWIP	724	220	352	454	541
Intangible assets	122	494	494	494	494
Deferred tax assets, net	0	0	0	0	0
Other assets	297	1,045	1,673	2,154	2,570
Total assets	28,457	42,772	63,690	82,347	100,279

Cash Flows

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Cash flow from operations	1,701	2,728	1,471	6,189	5,972
Capital expenditures	(1,680)	(4,174)	(2,500)	(2,500)	(2,500)
Change in investments	(949)	(452)	0	0	0
Other investing cash flows	(26)	(19)	722	553	479
Cash flow from investing	(2,654)	(4,645)	(1,778)	(1,947)	(2,021)
Equities issued/Others	269	642	0	0	0
Debt raised/repaid	688	2,174	493	739	640
Interest expenses	0	0	0	0	0
Dividends paid	(322)	228	(119)	(119)	(119)
Other financing cash flows	0	0	0	0	0
Cash flow from financing	635	3,043	374	621	522
Chg in cash & cash eq.	(318)	1,126	67	4,862	4,472
Closing cash & cash eq.	1,641	3,174	3,241	8,103	12,576

Per Share

Y/E 31 Mar (Rs)	FY21A	FY22A	FY23E	FY24E	FY25E
Reported EPS	26.9	32.1	59.9	85.0	103.8
Adjusted EPS	26.9	32.1	59.9	85.0	103.8
Dividend per share	1.0	2.0	2.0	2.0	2.0
Book value per share	124.2	168.0	225.9	308.9	410.7

Valuations Ratios

Y/E 31 Mar (x)	FY21A	FY22A	FY23E	FY24E	FY25E
EV/Sales	4.0	2.4	1.5	1.2	1.0
EV/EBITDA	89.0	67.2	38.5	28.8	24.0
Adjusted P/E	159.5	133.9	71.7	50.5	41.4
P/BV	34.6	25.6	19.0	13.9	10.5

DuPont Analysis

Y/E 31 Mar (%)	FY21A	FY22A	FY23E	FY24E	FY25E
Tax burden (Net profit/PBT)	73.6	74.7	74.8	74.8	74.8
Interest burden (PBT/EBIT)	89.4	86.3	91.5	93.0	93.6
EBIT margin (EBIT/Revenue)	3.8	2.8	3.0	3.3	3.3
Asset turnover (Rev./Avg TA)	11.9	11.2	16.1	19.1	21.6
Leverage (Avg TA/Avg Equity)	0.8	1.1	0.9	0.7	0.6
Adjusted ROAE	25.0	22.0	30.4	31.8	28.8

Ratio Analysis

Y/E 31 Mar	FY21A	FY22A	FY23E	FY24E	FY25E
YoY growth (%)					
Revenue	46.5	65.9	60.1	28.7	19.3
EBITDA	28.5	32.3	74.8	33.4	20.3
Adjusted EPS	32.6	19.1	86.8	41.9	22.1
Profitability & Return ratios (%)					
EBITDA margin	4.4	3.5	3.9	4.0	4.0
EBIT margin	3.8	2.8	3.0	3.3	3.3
Adjusted profit margin	2.5	1.8	2.1	2.3	2.3
Adjusted ROAE	25.0	22.0	30.4	31.8	28.8
ROCE	23.8	19.1	23.7	25.6	24.1
Working capital days (days)					
Receivables	62	46	50	48	49
Inventory	42	39	40	40	40
Payables	97	79	79	79	79
Ratios (x)					
Gross asset turnover	11.3	11.8	13.4	14.4	14.8
Current ratio	1.2	1.2	1.2	1.2	1.3
Net interest coverage ratio	8.9	6.7	10.8	13.1	14.4
Adjusted debt/equity	0.2	0.5	0.4	0.3	0.3

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Disclaimer

Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

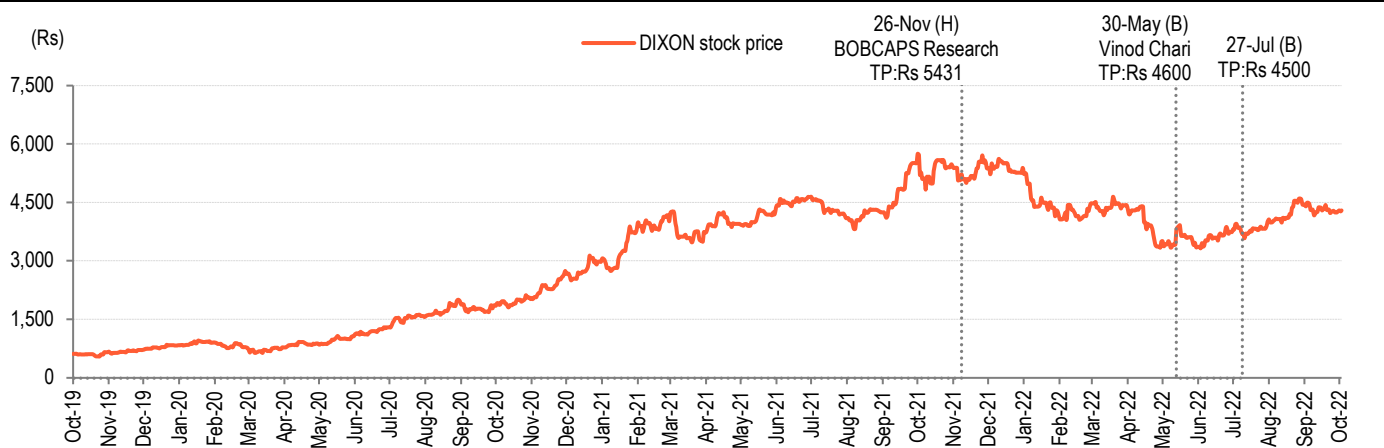
HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

Ratings and Target Price (3-year history): DIXON TECHNOLOGIES (DIXON IN)



B – Buy, H – Hold, S – Sell, A – Add, R – Reduce

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