January 17, 2023

Padget Electronics Pvt. Ltd.: ICRA]AA- (CE) (Stable)/ [ICRA]A1+ (CE) withdrawn and fresh rating of [ICRA]AA- (Stable)/ [ICRA]A1+ assigned simultaneously; rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term – Fund-based – Others	0.00	210.00	[ICRA]AA- (Stable); assigned
Long-term – Fund-based – Term Loan	55.00	105.00	[ICRA]AA- (CE) (Stable) withdrawn and [ICRA]AA- (Stable) assigned simultaneously
Short-term – Non-fund based – Others	155.00	685.00	[ICRA]A1+ (CE) withdrawn and [ICRA]A1+ assigned simultaneously.
Total	**210.00**	**1,000.00**	

**Instrument details are provided in Annexure-I*

Rationale

ICRA has withdrawn its ratings of [ICRA]AA-(CE) (Stable)/ [ICRA]A1+(CE) for the bank facilities of Padget Electronics Private Limited (PEPL) and has simultaneously assigned fresh ratings of [ICRA]AA- (Stable)/ [ICRA]A1+ for these facilities. ICRA has also assigned [ICRA]AA-(Stable)/[ICRA]A1+ for the enhanced bank limits of PEPL.

The withdrawal of the CE ratings is triggered by the Guidance Note and the FAQ document issued by the Reserve Bank of India (RBI) to credit rating agencies on April 22, 2022 and July 26, 2022, respectively, guiding that the benefit of a corporate guarantee that does not meet the evaluation mechanism/criteria defined by the RBI is not to be considered while assigning credit enhanced (CE) ratings. The [ICRA]AA- (CE) (Stable)/ [ICRA]A1+(CE) ratings drew comfort from the presence of a corporate guarantee extended by Dixon Technologies (India) Limited (DTIL) to the lenders of the rated bank facilities of PEPL. For assigning the earlier CE rating, ICRA had assessed the attributes of the guarantee issued by DTIL in favour of the rated facilities. While the guarantee was legally enforceable, irrevocable, unconditional, covered the entire amount and tenor of the rated facility, and met all the attributes of a strong guarantee, it did not have a well-defined invocation and payment mechanism. Taking cognisance of the above, ICRA assigned a rating of [ICRA]AA- (CE) (Stable)/ [ICRA]A1+(CE) to the said facility against the unsupported rating of [ICRA]A- /[ICRA]A2+.

To align itself with the aforesaid regulatory guidance, ICRA would no longer be considering in its credit assessments the benefit of a guarantee that lacks an invocation and payment mechanism, though such a support represents a relatively stronger expression of commitment on the part of the support provider for the supported facilities in comparison to a support that is only implicit in nature.

Yet the rating level for the bank facilities of PEPL (assigned afresh and being conveyed through this release) remains unchanged because of the change in ICRA's analytical approach. For arriving at the ratings, ICRA has now taken a consolidated view of PEPL along with its parent, DTIL.

The change in approach is based on ICRA's view that PEPL is an integral part of DTIL and operates like an extended arm of DTIL. ICRA draws comfort from DTIL's track record of support to PEPL and the close business, financial and management linkages between both the entities. ICRA takes note of common treasury team and representation of various directors of DTIL on the board of PEPL as well. Over the years, the share of PEPL in DTIL's consolidated revenue has increased, further highlighting increased strategic importance of PEPL for the parent entity. ICRA expects the linkages between DTIL and PEPL will remain strong on various dimensions, including business ties, financial aspects, and management support—that reinforce the application of the consolidated view approach.

The ratings factor in the robust growth in DTIL's scale of operations in the recent past (at a five-year CAGR of 34%), which imparts economies of scale benefit. The ratings note DTIL's established track record as an electronic manufacturing services (EMS) player with presence in diversified product segments and leading position in its key product segments (like LED television, lighting, etc), along with its well-established relationship with reputed clients. The ratings favourably consider DTIL's strong return on capital employed (RoCE) and comfortable debt coverage indicators with an interest cover of 7.8 times in FY2022 and the same is expected to remain above 6 times during FY2023. 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. While its revenues are expected to increase by around 30% in FY2023, the operating margins are likely 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 its 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 TOL[1]/TNW of 3.3 times as of March 2022, which is expected to remain below 3.5 times in FY2023, 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.

ICRA notes that 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 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. 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 and are expected to sustain at the current levels during FY2023. However, supported by expansion in scale of operations and increasing share of Original Design Manufacturer (ODM) business with better operating profitability, the OPM is expected to improve gradually 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 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.

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[1]*Adjusted for unencumbered liquidity*

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, wherein it operates, i.e., LED television, lighting, and washing machine. Over the years, the company has augmented its manufacturing capacities and acquired 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 (STBs) and medical electronics. While the CE, lighting, and home appliances segments are catered by DTIL, mobile phones and medical electronics manufacturing come under its subsidiary, Padget Electronics Private Limited (PEPL; erstwhile joint venture/JV). Security devices 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 and H1 FY2023. 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 and H1 FY2023, 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 ~44% in H1 FY2023 (over H1 FY2022). 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 driven by healthy accruals from operations and issuance of employee stock option programme. However, the external borrowings have increased with the ongoing capex. The credit profile remains healthy as reflected in interest coverage ratio of 7.8 times in FY2022 and the same is expected to remain above 6 times during FY2023. 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 likely 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 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 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 on March 31, 2022) against reported TOL/TNW of 3.6 times. The net TOL/ TNW is expected to remain below 3.5 times during FY2023. The creditor as well as TOL are likely to increase over the medium term, given the strong revenue growth expectations. 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. Nevertheless, 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. The industry players are required to undertake continuous upgrades to sustain the competitive advantage, given the risk of technological obsolescence. 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 due to sizeable imports. However, the forex risk is abated to an extent by its 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. 260.21 crore as on September 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 a mix of external debt and 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 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 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 Policy on Withdrawal of Credit Ratings Rating Approach - Consolidation
Parent/Group support	Not Applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of DTIL

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 into 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. DTIL is listed on both the National Stock Exchange (NSE) and Bombay Stock Exchange (BSE). In FY2022, it 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. In H1 FY2023, the company reported a net profit of Rs. 123.2 crore on an OI of Rs. 6,721.8 crore (44% higher against H1 FY2022).

Padget Electronics Private Limited (PEPL) is a 100% subsidiary of DTIL that manufactures/assembles mobile handsets and STBs. Its manufacturing facility is located in Noida and it started production of mobiles in November 2015. The company was initially established as a JV between DTIL and the Jaina Group (owners of Karbonn brand), in 2013. DTIL, on April 12, 2019, acquired the balance 50% equity share of PEPL from Mr. Pradeep Jain (holding ~47% shares of PEPL on March 31, 2019) and other Jaina Group companies (holding ~3% shares of PEPL on March 31, 2019) for Rs. 27 crore in an all cash deal.

An application made by PEPL for license as a domestic manufacturer of mobile phones, under the India's Government's PLI scheme, was accepted in October 2020. It is one of the few companies to achieve the eligibility criteria and receive the incentive. The company has entered into the manufacturing agreement with global brands like Motorola and Nokia for production of mobile phones for sales in both domestic market and as well as export markets.

Key financial indicators (audited)

DTIL Consolidated	FY2021	FY2022	H1FY2023
Operating income	6,448.2	10,697.1	6,721.8
PAT	159.8	190.4	123.2
OPBDIT/OI	4.5%	3.6%	3.6%
PAT/OI	2.5%	1.8%	1.8%
Total outside liabilities/Tangible net worth (times)	3.0	3.6	3.5
Total debt/OPBDIT (times)	0.8	1.9	0.8
Interest coverage (times)	8.9	7.8	8.1

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

Instrument		Current rating (FY2023)					Chronology of rating history for the past 3 years		
		Type	Amount rated (Rs. crore)	Amount outstanding as on Dec 31, 2022 (Rs. crore)	Date & rating in FY2023		Date & rating in FY2021	Date & rating in FY2020	Date & rating in FY2019
					January 17, 2023	June 30 ,2022	Mar 17, 2021	-	-
1	**Fund-based – Others**	Long term	210.00	-	**[ICRA]AA- (Stable**	-	-	-	-
2	**Fund-based – Term Loan**	Long term	105.00	76.3	**ICRA] AA- (CE) (Stable) withdrawn and [ICRA]AA- (Stable) assigned simultaneously**	**[ICRA]AA-(CE) (Stable)**	**[ICRA]AA-(CE) (Stable)**	-	-
3	**Non-fund based – Others**	short term	685.00	-	**[ICRA]A1+ (CE) withdrawn and [ICRA]A1+ assigned simultaneously**	**[ICRA]A1+(CE)**	**[ICRA]A1+(CE)**	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term – Fund-based – Others	Simple
Long-term – Fund-based – Term loan	Simple
Short-term – Non-fund based – Others	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: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Fund-based – Term loan	Feb 14, 2020	NA	Feb 28, 2025	105.00	[ICRA]AA- (CE) (Stable) withdrawn and [ICRA]AA- (Stable) assigned simultaneously
NA	Non-fund based – Working capital facilities	NA	NA	NA	685.00	[ICRA]A1+ (CE) withdrawn and [ICRA]A1+ assigned simultaneously
NA	Fund-based – Others	NA	NA	FY2026	210.00	[ICRA]AA-(Stable)

Source: Company

Please click here to view details of lender-wise facilities rated by ICRA

Annexure II: List of entities considered for consolidated analysis

Company Name	DTIL 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: DTIL annual report FY2022

Note: ICRA has taken a consolidated view of the parent (DTIL), its subsidiaries and associates while assigning the ratings.

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

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