Buy & forget stock idea - "Dixon Technologies – 2nd largest (9% market share) EMS company in India" might be 20X bigger than its current size of 2000 Cr Market Cap (35% cagr over next 10 years)

[Best buying range = 1800-2000 | Portfolio allocation = 5-8%]

Dixon Technologies (India) (DTIL) is the largest home-grown, design-focused and solutions company engaged in manufacturing products in consumer electronics (LED TV), home appliances (Washing Machine), security systems (DVR, CCTV), lighting solutions (LED/CFL), mobile phones & reverse logistics in India. *More and more brands are focusing on branding alone; distribution and manufacturing are mostly outsourced.* In next 3-5 years India is going to be a major electronic manufacturing hub globally apart from China and Vietnam (emerging). With increasing cost of labour in China, favourable policies of Indian government and levy of import duties, most of the brands prefer domestic sourcing of their consumer products.

Following are the reasons why we are very bullish on this counter…

1) Outsourcing of manufacturing is a BIG trend – There is rising preference of OEM brands to outsource products from EMS players instead of in-house manufacturing. Dixon is likely to be a major beneficiary of this new trend owing to its leading market share in most of their core sub-segments. With reputed anchor clients in categories such as LED TVs, lighting, washing machines, security systems, mobile phones and reverse logistics solutions, DTIL offers strong long-term growth prospects.

2) EMS industry has strong (30% plus) growth prospects – Due to factors such as high demand, rising aspiration of consumers, rising affordability, availability of easy financing schemes and low penetration level across product categories. While the consumer electronics industry is poised to post 17% CAGR over FY16-FY21E, the EMS industry will outpace its growth with 31% CAGR owing to rising preference of OEM brands to outsource products from EMS players instead of in-house manufacturing. Believe me everyone wants to own the brand (high margin), but no one wants to manufacture (low margin).

3) An asset-light balance sheet with strong return ratios – Low working capital cycle, stable operating cash flows and high returns coupled with availability of adequate capacity makes this company an attractive play in an exciting industry. The revenue and reported net profit have grown at a CAGR of 30% and 62% respectively since last 5 years. While the EBITDA margin of DTIL appears to be low at 4% in FY18, it must be noted that DTIL earns only a conversion charge in OEM business and hence the percentage margin is not the correct indicator of its profitability. The ideal tool to judge profitability is RoCE which is strong at 34% in FY18. In FY14-FY18, EBITDA &

PAT grew at a faster pace of 37% & 34% CAGR, respectively, versus 30% revenue CAGR.

4) DTIL has market leadership in three core segments - DTIL has strong leadership position in three sub-categories of EMS industry, namely LED TVs (50% market share), semi-automatic washing machines (42% share) and LED/CFL lights (38% share). With economies of scale, highest market share and a healthy track record of manufacturing products for reputed brands (Panasonic and Philips), DTIL is likely to be the preferred EMS partner for any OEM brand looking to enter or enhance its offerings in these categories.

5) Risk-free business with operating leverage - They pass on any impact of cost or currency to the customer as per the contract. They have built very large capacity so the operating leverage advantage would start kicking in and in all the verticals there is a significant migration to ODM which will help improve operating margin. Recently Xiaomi partnered with Dixon Technologies to manufacture Mi LED TVs in India. The company has all the big brands in LEDs in its basket, it has added Orient, Syska, Bajaj, Usha, Jaguar and expanded lighting product portfolio with Wipro High Beam LED Bulb.

6) Most of the marquee brands are their customers – A major part of DTIL's revenues and operating profitability is derived from its top two customers – Philips, and Panasonic. However, this is not a risk because of their long relationship with the clients (Phillips – 9 years and Panasonic – 5 years) and their strong patronage. For Samsung, Dixon is the only partner as far as washing machine is concerned. Xiaomi, Dixon is the only partner as far as TV is concerned. Panasonic, Dixon is the only partner for TV, for washing machines, mobile phones and almost 80% of their bulb requirement. For Skyworth, PCL or BPL, Flipkart we are the only partner. Philips almost 80% of the indoor lighting is only through Dixon. In short, Dixon commands good reputation among top notch clients & can be a reliable partner. Key customers include Panasonic India, Philips Lighting India, Haier Appliance (I), Gionee, Surya Roshni, Reliance Retail, Intex Technologies (I), Mitashi Edutainment, Dish Infra Services, Vijay Sales etc.

7) ODM model and reverse logistics are key margin drivers - Rising share of ODM model where product development and designing are done in-house by DTIL (21.3% of FY18 sales) and reverse logistics solutions (2.5% of FY18 sales) are key drivers of profitability with EBITDA margin of 9% and 18%, respectively, in FY18.

Date : Jan 2019