



“Dixon Technologies (India) Limited 3QFY21 Earnings Conference Call”

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MODERATORS: MR. DHRUV JAIN – EQUITY RESEARCH ANALYST, AMBIT CAPITAL

Moderator: Ladies and gentlemen, good day and welcome to the Dixon Technologies India Limited 3QFY21 earnings conference call hosted by Ambit Capital.

As a reminder, all participants' lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touch-tone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Dhruv Jain from Ambit Capital. Thank you and over to you, sir.

Dhruv Jain: Hello everyone. Welcome to the Dixon Technologies 3QFY21 earnings call. We have with us Mr. Atul Lall - Vice Chairman & Managing Director of Dixon, and Mr. Saurabh Gupta - CFO of the company. Over to you, sir, for your opening remarks.

Atul B Lall: Good afternoon ladies and gentlemen. This is Atul Lall and we also have on the call today our CFO Saurabh Gupta.

Saurabh Gupta: Good afternoon everybody.

Atul B Lall: Thank you very much for joining this Earnings Call for the quarter ended December 2020. Wishing you all a very happy new year. I am delighted to share that we had a good all-round performance during the quarter with highest ever revenue and profitability.

The consolidated revenues for the quarter ended December 31, 2020 was Rs2,183 crores as against Rs994 crores in the same period last year. That's a growth of 120%. Consolidated EBITDA for the quarter ended December 31, 2020, was Rs100.6 crores as against Rs53.4 crores in the same period last year, which is a robust growth of 89%. Gross margins and EBITDA margin contraction year-on-year was primarily driven by a substantial change in the segment mix with a higher increase in share of business during the quarter from LED TVs and also due to certain input price increases.

Large scale enabled us to generate a better operating leverage to offset some of the gross margin contraction due to increasing input prices. Consolidated PAT for the quarter ended December 31, 2020, was Rs. 61.6 crores against Rs. 26.3 crores in the same period last year, which is a strong growth of 134%. Friends, the growth has been broad based with secular growth across all the divisions led by improvement in consumer sentiment, festive season, reduction in Covid-19 cases and also strong manufacturing base.

The order book in the current quarter and forecast for the forthcoming fiscal continues to be very strong. The results also demonstrate, my friends, the durability of our business model as well as our strong execution capabilities while the overall demand outlook has improved significantly, and the growth is reflected across businesses.

We are currently facing headwinds in terms of increased commodity cost. Sudden surge in demand coupled with few supply side issues led to global trade mismatch for many commodities resulting in sharp price inflation as well as occasional shortage of material. We expect the cost pressure to continue in the near to mid-term which will pose a challenge to our ODN business model. However, our frugal cost structures and large scale gives us a competitive edge in this difficult situation also.

We are continuing to monitor the situation closely and address the margin pressure in our ODM business through combination of calibrated price increases and also focus on inventory planning. So, we have always been focusing on very prudent capital allocation, building large scale to generate operating leverage, migrating more and more to our own design solutions, deepening relationships with existing customers, and acquisition of new customers.

Further, whenever the opportunity comes, we are entering in the new domains, however, without losing the focus on our capability and core competence in electronics manufacturing.

Also, in certain verticals, we see that we are globally competitive and also have technical bandwidth to start exploring the global markets. We are well positioned with a robust balance sheet with a cash balance of 151 crores, net debt of negative 54 crores as on 31st December '20. Our balance sheet strength enables us to weather any future uncertainty and also invest in the long-term development of our business. It has enabled us to invest to continue to invest in our organization and people through this entire challenging period of Covid. We also continue to step our investments in people in hiring and development of our R&D capabilities. I am sure the benefits of this which are already showing results is going to further strengthen our business in the long term. In addition, strong return ratios have been maintained with an ROE of 23.8% and ROCE of 31.7% at the end of Q3 '20-21.

We will continue to focus on 3 drivers of future cash flow, earning expansion, working capital efficiencies, and extremely disciplined investment in capital allocation.

Now, I will share with you the performance and the strategy in each of the verticals going forward.

I start with LED television, i.e., consumer electronics. Revenues for the quarter under review was Rs. 1360 crores against Rs. 454 crores in the same period last year. That is a robust growth of 199%. This has been led both by volume and pricing growth.

Operating profit also saw a significant increase of 243% year-on-year. So, we generated an operating profit in this quarter of 39.4 crores against Rs. 11.5 crores in the same period last year. Operating profit margins also expanded from 2.5% to 2.9% year-on-year. This is on account of operating leverage, higher level of backward integration through the PCBA route, improved sales mix from larger screen sizes, i.e., 43 inches and above as against 32 inches with better margins. Growth has also come in because of government policy intervention wherein the LED TVs were shifted from OGL to the restricted category.

We presently have a capacity of 4.4 million sets including backward integration in LCM and SMT lines. This is already the largest capacity in India. It is almost 30% of India's LED TV requirement. The order book and forecast from our customers continues to be very healthy. As I had mentioned in the last earning calls, we are further expanding our capacity to 5.5 million sets which I am confident will be completed by Q2 of next fiscal to cash the festive period. This will be done by adding an automated 65 inches integrated line with LCM and FA to meet the customer demands. With this increased capacity, we will have a large share of Indian requirement equivalent to almost 40%. Further, we are adding our SMT capacity and the PCBA capacity which has already been increased from 1 million to 1.8 million by Q2 of next fiscal will be increased to 2.8 million. Now we have a total area of half a million square feet in our integrated campus at Tirupati which is fully backwardly integrated. Further, we are backwardly integrating even more because we have traction and an instruction from our customer to start doing the injection molding and also the backlight assembly. So, in India, we are, in fact, the most vertically integrated LED TV plant. Further we will strengthen our R&D team and we have already developed new cost-effective solutions for both analog and smart TVs. We have also developed the entire TV solutions and now we are working with Google to cover up the IT issues.

Next, coming onto lighting:

The revenues for the quarter witnessed a growth of 26% year-on-year. We did have revenue of 349 crores in Q3 of '20-21 against 277 crores in the same period last year. Within a very short span of time, our lighting business has exceeded pre-Covid growth levels and is back to the strong growth trajectory which we have been demonstrating. Operating profit also witnessed a significant growth of 39% year-on-year. We had an operating profit of 33 crores in Q3 of '20-21 against 34 crores in the same period last year. The margins in the lighting business have further expanded from 8.6% to 9.5%. This is again due to operating leverage migrating more to our own design solutions, value engineering, productivity improvement, and better product mix. Practically, all the brands in lighting are our customers today and they are all on ODM basis. Also, most of the customers we have a very large share of their wallet. We are presently India's largest ODM in lighting and we have a capacity of LED bulbs of 300 million which is almost 45% of the Indian requirement. We have also developed solutions for smart LED bulbs, battens, downlighters, and emergency bulbs for various customers.

In the case of battens, we have already expanded our capacity to 2 million per month. Our order book is very healthy. So, we are further expanding our capacity in phase-I to 3 million and then to 4 million. This will again be almost 40% to 45% of the Indian requirement. Also, in downlighters, the order book is very healthy. So, we expanded our capacity from 600 k per month to 1.2 million per month in this phase. Also, we have created a capacity of 5 million per month for 0.5 V decorative lamps.

The order book, friends, is very good. Therefore, we have decided to set up another factory for lighting. That is going to be in the hinterland so that the capital allocation again is very frugal.

The sites are being explored and we have almost finalized on 1 site to set up this new factory and hopefully this should be operative by Q3 of the forthcoming fiscal.

We feel with the kind of volumes in the entire range of product portfolio, we are now globally competitive and amongst the top companies in the world as far as volume is concerned in certain SKUs, we have the cost competitiveness and also the technical bandwidth. We have already started exporting for our anchor customers to US and Indonesia, and we are in discussions with some very large retail chains globally. We are confident that in the next couple of quarters, we are going to have significant breakthroughs in getting large accounts for export of LED bulbs. We have also completed automation of one-third of our capacity for LED bulbs, which will have a reduction in our manufacturing cost and boost productivity. Further, the R&D teams are developing the outdoor lighting solutions, mainly the streetlight, and this product portfolio will be launched by Q2 of the coming fiscal.

The third vertical, home appliances:

Revenues for the quarter saw a good growth of 68% year-on-year. From 68 crores in Q3 of '19-20, it has increased to 115 crores in Q3 of '20-21. The operating profit, however, has increased by 28% year-on-year which is lower than the revenue growth. It has grown from 9 crores in Q3 of '19-20 to 11.8 crores in Q3 of '20-21. This has been primarily because of increase in the input prices and also the improved freight rates. There is a certain lag in passing on this price increase. So, the margins for the current quarter also would be under some pressure, but we are hopeful that from the next quarter, we will be back to normal. The order book in this particular vertical again continues to be very high, very good for the current quarter also. So, we have decided to expand our capacity at a new site in Dehradun in an adjacent plot of land wherein we are going to expand the capacity of semi-automatic from 1.2 million to almost 1.6 million. We have the largest product portfolio right from 6 kg up to 11.5 kg, and also we have more than 170 models which is the largest product portfolio either with any brand owner or with any outsourcing company.

Our plant in Tirupati campus for fully automatic top loading is almost complete. The lines are being laid and the trials will begin from February end or early March. This is the complete product portfolio with a capacity of almost 600 k per year. The combined capacity in 2 plants is going to be 2.2 million against the Indian demand of 7 to 7.5 million. We will have almost 30% capacity with the largest product portfolio and a footprint both in north and south. So, we are confident that finally it is going to take some time, but it is going to be an extremely important kind of strategic vertical for us.

Coming to the next vertical of mobile phones & EMS division, this quarter onwards, we will start reporting our mobile and EMS division revenues and profitability combined. Revenues for the quarter under review was 299 crores as against 140 crores of mobile revenues in the same period last year, which is a growth of 114%. In the current quarter, the revenues of set top boxes and medical equipment was Rs. 69 crores and Rs. 11 crores respectively of the 299

crores. Operating profit also witnessed a strong growth of 328% at Rs. 13.8 crores against Rs. 3.2 crores in the same period last year, which is primarily on account of contribution of our anchor customers 2G phone, set top box, and medical electronics business. Also, operating margins expanded from 2.3% to 4.6% year-on-year.

We have the largest capacity of 2.3 million 2G phones per month for our anchor customers, which is being used for both exports and domestic markets. We have a very heavy order book from our anchor customers of 2G phones and this will not be a part of the mobile PLI scheme.

We have already closed agreements with new global customers, global brands Motorola and Nokia. The commercial production for Nokia has already started. For Motorola, the audits are happening and we are confident that the commercial production will start by the end of February or early March. The new factory under the PLI scheme has already been set up. The trials are happening, and to meet the eligibility criteria of 50 crores of CAPEX to get the PLI benefits has already been met.

Finally, our capacity for smartphones annually in the next couple of years is going to be almost 20 million per annum. We think it is a very big opportunity for us and we are very confident of generating a cumulative revenue of around 25,000 to 28,000 crores over a period of 5 years with 3% kind of EBITDA and a robust ROC after some ramp up challenges and then a quick payback on the investments. We are confident that we will be delivering revenues much beyond the ceiling limits for each of the years starting '21-22 as per the forecast from our customers.

We also have an advantage as compared to our competition that we are one company which is purely focused on manufacturing and EMS activity and there is no clash of other competition which is promoting its own brand also. Further, as we have done in other verticals, we will be seriously exploring the backward integration of chargers, batteries, and mechanicals in this particular category also.

In set top boxes, we manufactured 9 lakh set top boxes for Jio, Dish TV, and City Cable in and reported revenues of 69 crores. We have a very healthy order book of approximately 3 to 4 lakhs a month for the forthcoming quarters.

Medical electronics, we have manufactured 500 units of the RT-PCR machine for Molbio. Revenue for the quarter under review was 11 crores with a healthy operating margin of almost 28%, an extremely high ROC.

Further, we have got into a new domain of wearables, i.e., mainly TWS. This is our tie-up with boAt and we have got an initial order of 10,000 units and the manufacturing for this particular product will start from February itself. We understand that the government is rolling out a PLI scheme for wearables, which will be definitely studying and pursuing.

Coming to the next vertical of security surveillance systems:

There is a 10% year-on-year growth and 40% sequential growth in our share of 50% revenues to Rs. 55.5 crores with an operating margin of 3.5%. In my last interaction with you, I had shared that the demand in this particular vertical was under pressure. However, I am pleased to inform you that it has recovered extremely well and we have a very very healthy order book. As per the forecast, we are further expanding our capacity in this vertical also.

Last but not the least, our vertical of reverse logistics, the revenue for the quarter in this particular vertical was Rs. 4.5 crores and an operating profit of Rs. 46 lakhs. Mainly, this is for set top boxes and LED TV panel repair business and now we have opened up a new center for reverse logistics in Tirupati also because this is more of a strategic kind.

I would like to stop now and here me and Saurabh are there to respond to your questions. Thank you.

Moderator: Ladies and gentlemen, we will now begin the question & answer session. We will wait for a moment while the question queue assembles. The first question is from the line of Vihang Subramaniam from Samsung Asset Management. Please go ahead.

Vihang Subramaniam: Just 2 quick questions. On the PLI, we have signed up with, I guess, Nokia and Motorola, right? Just wanted your thoughts on why these brands versus other brands like Xiaomi, etc. I kind of had the impression that these are sort of weaker brands. Just your thoughts on this, and how would this business look post PLI, like post FY25?

Atul B Lall: These are the first 2 customers that we have finalized, and customer acquisition is an ongoing process. Further, the order book and the forecast given by Motorola is itself consuming almost most of the ceiling that the government offers. Also, in Motorola's case, a large part of revenue is going to be generated from the global markets. So, we are of a firm conviction that this business relationship is on an extremely strong footing, and we are fairly confident that it is going to extend beyond the PLI times. It is a huge deepening of the relationship.

Second question is how beyond the PLI period of '24-25, this business is going to be sustainable. We feel that 4 to 5 years is good enough a time wherein the government is supporting the industry in its infancy stage. And this is the time when more deepening of manufacturing will happen in India, more backward integration will take place within Dixon and in India, and the country and so is the case going to be with Dixon that they are going to be globally competitive without any PLI available. This is the way it works with most of the industries, and we feel that it is going to happen in this particular vertical for Dixon also.

Vihang Subramaniam: Any thoughts on why these customers versus like other ones like Xiaomi or Samsung?

Atul B Lall: There is already a large relationship between us and Samsung. We are already there. We are their supplier of a complete quantity of 2G phones. And also please appreciate for smartphones, Samsung already is also a beneficiary under the PLI scheme. Now, why not

Xiaomi and why Motorola and Nokia? Well, again I say and I can't share more that customer acquisition is a continuous exercise. Nothing stops at Nokia and Motorola.

Vihang Subramaniyam: My second question on TV, you mentioned that now you are 40% of the market, right? So, at what percent of the market do you think you can go up to after which you will be growing in line with the end market?

Atul B Lall: This year, in spite of the pandemic, we are going to close almost at 2.9 million to 3 million sets. And last year, we did around 2.1 million sets. So, we feel that we will continue to grow at 20% to 25% this year also. However, to be very candid and transparent, the issue today is not with the order book. The issue as of now is with the supply chain challenges that globally the availability of open cell and glass is under huge pressure and we feel that at least for a quarter or so if not more, it will continue to be under pressure. So, in Dixon's case, in the television vertical, growth we are fairly confident it will come and we should have a good number in the forthcoming fiscal also. Now, how it pans out after that? We still have to wait and watch because we have a large share of the Indian players and the other large players are already doing their in-house manufacturing or with some other large partners. So, one will have to wait and watch and see for that.

Vihang Subramaniyam: Just the last bit from my side. On lighting, you are expanding your capacity in battens and downlighters. By which year, you think this capacity will be completely utilized? Would it be like FY22 or FY23, any sense on that?

Atul B Lall: Our order book is extremely strong. In fact, there has been some mismatch that we did not anticipate this kind of an order book. So, we already have the order book for utilizing this capacity. We have to really rush in getting this footprint ready.

Moderator: The next question is from the line of Ravi Swaminathan from Spark Capital. Please go ahead.

Ravi Swaminathan: Congrats on a good set of numbers.

Atul B Lall: Thank you, Ravi.

Ravi Swaminathan: In continuation with the previous question - In LED TV, if you can give what is the current market size this year? And you told around 2.9 million to 3 million pieces we are doing currently and you told we are also doing the higher inches, i.e., 43 inches and above. What is the opportunity there and is there any export opportunity which can be given? This is my question. My second question is with respect to the wearables - how much amount of potential revenue that we can get from the wearables? If you can give that outlook also, it will be great, sir.

Atul B Lall: On the LED TV side, the market has shifted from 32 inches to 43 inches. So, the unit value of our sales which used to hover at around Rs. 9000 to Rs. 10,000 has increased to almost Rs. 14,000 to Rs. 15,000 in the last 2 quarters. That's a significant jump. Also, volume-wise, we

have an extremely healthy order book because we have been continuously acquiring customers. Starting with Xiaomi, we added Samsung; we added private labels of Flipkart, Nokia, and Motorola; we have added Reliance's private label; we have added BU; we have Tata Croma. Continuously we are adding, and we are also expecting some more customer acquisitions in the forthcoming quarters. Both revenue-wise and unit value-wise, margin expansion-wise, and backward integration-wise, I think we are on a healthy wicket. And '21-22 looks to be fairly good, in fact, very good. Now, whether there is any potential for export, I don't think there is any potential for export because until and unless there is an open cell fab in India, as a country, I don't think we are there for export of LED televisions.

On the wearables side, our understanding is that the market is approximately 5000 crores but it is growing at a very fast pace and we are tied up with both. Both have an extremely smart and aggressive management team. Within a very short period of time, we have been able to create an extremely good and iconic kind of a brand not only for the domestic market but for the global market also. It is still too early to forecast the numbers, but I have a good feel about this as well. I am not in a position to share the numbers as such but I think it is going to be a good, strong, robust relationship.

Ravi Swaminathan:

The second question is with respect to the PLI scheme. I read in news articles that for the FY20 base year, the companies have requested to get it shifted to FY21. Is it likely to get stuck with FY20 itself as a base or FY21 is it likely to be rolled forward and is there any implication because of that?

Atul B Lall:

FY20-21 because of the supply chain constraints both on a display and the microprocessor side, nobody will be meeting the thresholds. So, the industry has requested the government for some kind of flexibility and extension. We are still waiting for the government's response. Let's see how it pans out. For the next year '21-22, the threshold is 1000 crores, which we are very confident to meet fairly soon both on the sides of threshold revenue as well as the CAPEX for meeting the eligibility criteria.

Moderator:

The next question is from the line of Abhishek Ghosh from DSP. Please go ahead.

Abhishek Ghosh:

The first question is in terms of Motorola, you mentioned the audits are on. Just wanted to get a sense since these are mostly for overseas volumes, what kind of overall... because I believe Motorola does about 40-41 million kind of handsets. What kind of market share or production share that you envisage to get it over a 2-3 year framework? How should one look at it from that perspective?

Atul B Lall:

My sense is that by year 3 or year 4, at least 15% to 20% of global requirement of Motorola should be with us.

Abhishek Ghosh:

In terms of Nokia again, is that number going to be similar, because their volumes are far lower, or is it mostly for the domestic market for the Nokia PLI that you have signed?

- Atul B Lall:** Nokia, to start with, is for the domestic markets. We have had some initial discussions for the exports but it is going to be step by step.
- Abhishek Ghosh:** There are a couple of more guys whom you are talking to in terms of mobile PLI, is it?
- Atul B Lall:** Yeah, we are in very advanced stages of discussions with some of the larger global brands. I am not in a position to share more details; yeah, but we are in discussions.
- Abhishek Ghosh:** Sir, just one last question. In your sense, where is this production getting shifted to? In terms of Motorola, they must be already producing in some part of the world. Where is the shift and if you can just help us understand that?
- Atul B Lall:** You are talking about shifting of the global footprint?
- Abhishek Ghosh:** Yeah, the global production shift that is happening. If they are going to give you the 15% to 20% of it, where will the shift happen from?
- Atul B Lall:** At present, if you see the global footprint of Motorola, it's presently in China, it's in Brazil, and for the domestic market, it was in India with one of the EMSs. So, I see the China production being shifted out to India for servicing the global requirement also.
- Moderator:** The next question is from the line of Aditya Bhartia from Investec. Please go ahead.
- Aditya Bhartia:** Sir, my first question is on the LED TV business. If you could just help us understand what proportion of our revenues would be coming from existing customers like Xiaomi, Panasonic, and others and what proportion possibly would be coming from new customers that we have acquired, and how the ramp up would happen?
- Saurabh Gupta:** In this quarter 3, between Xiaomi and Samsung, almost 75% of our revenues are coming and then balance 24% revenues are coming from the other brands.
- Atul B Lall:** I feel that with the addition of new customers, this 75% is going to come down to somewhere between 65% to 67% and balance is going to happen from other customers and new customers.
- Saurabh Gupta:** And also, to add to it, I will say since the same period last year, the top 2 customers last year were contributing almost 85%-odd. So, it has significantly de-risked to that extent, and as Mr. Lall mentioned, it will continue to get lower with more customer acquisitions.
- Aditya Bhartia:** As far as the Samsung contract is concerned, we have completely ramped up with the overall kind of volumes that we were looking for them - 500,000 to 600,000 units this year. Would we be achieving that?
- Atul B Lall:** We have been guided for volume of about 2.7 million in the forthcoming fiscal. We see that we should be achieving those numbers.

- Aditya Bhartiya:** Sorry, sir. I missed that.
- Saurabh Gupta:** Aditya, basically this year for Samsung, we should be closing somewhere around closer to 5 lakh kind of a number and next year we have been given an order book of somewhere around 7 odd lakhs.
- Aditya Bhartiya:** My next question is on the set top box business. How do you see the revenue potential for the set top box business and could there be an export opportunity out here?
- Atul B Lall:** We feel that the set top box business would be around 350 crores to 400 crores. And I don't see an export opportunity in set top box as of now. This is mainly for the domestic markets.
- Moderator:** The next question is from the line of Tejas Sheth from Nippon India AMC. Please go ahead.
- Tejas Sheth:** Two questions. We keep hearing that there is a huge supply chain issue on the chip side and even you also mentioned about the open cell. (1) How do you ensure that the supply chain for a new player like us, I mean in the PLI, gets a preference at the vendor level? (2) Do the brands help you in getting this supply chain process in place?
- Atul B Lall:** Tejas, there are 2 parts to this point. One is, you specifically asked in the context of mobiles in PLI. There the supply chain and the sourcing and procurement is managed by the brand owner to start with. So, we feel confident that with the clout of the large global brands like Motorola and also Nokia, they're overcoming that and I can see it falling in place. Then, the issues are hugely into the LED lighting, but I think we took a very prudent call back in September and October to accumulate inventory, particularly of driver IC and LED chips. We are one of the very few manufacturers which are able to execute the business and we continue to have the inventory and supply chain in place in spite of the problems. And that is another primary reason for consolidation and an increase in volumes and revenues in lighting for Dixon.
- In the case of televisions, there is a global slot for open cell. So, even the big ones like Samsung and Xiaomi are facing the challenges but let me assure you that they are much ahead of their peers in competition in sourcing their open cell so they are not at a level. The sale could have been much better if they had the complete quantity sourced but they are much ahead. So, in turn, Dixon is in a better situation as compared to competition.
- Tejas Sheth:** So, the onus of the supply chain getting in place is on the brands. Is it?
- Saurabh Gupta:** In the case of prescriptive business, Tejas. In LED lighting, we have to manage that.
- Tejas Sheth:** Second question. Now that the Motorola manufacturing or assembling has started, what are the service gaps which Motorola would want you to fulfill over the next 2 to 3 years when they compare you with their current sourcing from China? Are there any service gaps which they would want you to fulfill over the next 2 to 3 years?

Atul B Lall: First and the foremost is the technical ordered qualification and it's a very comprehensive audit. And Dixon, we are gearing up for it. We have qualified the first audit and now since the lines have been installed, the second audit and trial of their first 2 models is happening. Yeah, there are definitely initial challenges but we feel confident and we should be able to overcome that and the commercial production should start by the end of February or early March. This is what has to be sustained. They have an extremely close monitoring system both from China headquarters and their India teams. So, that deliverable is extremely important.

The second is on the aspect of the business processes. It's an American company with an American culture although with Chinese ownership now but the whole business processes flow from there. So, Dixon has to align and gear up for that.

Now, these two are extremely important deliverables on which Dixon will have to gear up and mature more to really reach the optimum level of customer satisfaction. These are going to be the most critical things apart from cost of course. Cost, I am very sure we will meet. So, if we are able to deliver on it - and we are working on it let me assure you - then I think the relationship can be taken to the next level.

Tejas Sheth: Just last in yesterday's budget had this tariff custom increase on the PCBs. I would just want to know at present, how much of the PCBs which we assemble are sourced in-house and 2-3 years down the line, what could this percentage be?

Atul B Lall: What the notification says is that the inputs for PCBAs as there is no duty increase. Now, most of the inputs for PCBA, they fall under the ITA-1 and the duty is 0% and the government cannot increase the duty. However, there are certain items like connectors or inductors on which there is an increase of duty. That's a very miniscule number. And in any case, for us, it's a pass-on. So, it's not that much of a challenge. On the other side, the duties have been increased on the inputs of chargers and batteries. In the short term, there will be some small cost increase for the mobile brands - not for Dixon, because it's a pass-on but it's in line with the government's efforts to deepen the manufacturing. So, I think that way, it's fine.

Tejas Sheth: No, I was just trying to understand, is there an opportunity for us to backward integrate further in the PCB components or even larger for that matter the whole PCB manufacturing over the next 2-3 years?

Atul B Lall: We are not looking at backward integration on that side. However, we will definitely be looking at the backward integration opportunities in the case of chargers, battery packs, and the mechanicals because that's our core.

Moderator: The next question is from the line of Naval from Emkay Global. Please go ahead.

Naval: Sir, congratulations for a good set of numbers. I have 2 questions; one on CAPEX, any number you want to state for FY21 and '22 as you are expanding capacity in various segments? And second, on lighting; as you have stated, there would be new facilities which you would be

setting up. Will that be under the upcoming PLI scheme or it would be separate from that? Lastly, Saurabh, if you can provide volume numbers for the quarter please.

Atul B Lall:

I will first respond on the lighting; and numbers is Saurabh's domain, he will discuss the numbers with you. From the lighting side, Naval, with or without PLI, in any case, we will be expanding our capacities. And in all probability, this facility will be coming up in Uttarakhand. Because the order book is extremely healthy and if you don't do it fast, we are going to lose the business and we are also going to hamper our relationship with our customers. Now we are expecting the PLI for lighting to be announced sometime by 2nd or 3rd week of February. We have been deeply interfacing with the government on the contours of that scheme, we are awaiting that scheme. And if it helps us in growing our business, which my sense is it will, we will be definitely pursuing it and we would align our new factory under the PLI scheme.

Saurabh Gupta:

Naval, on the CAPEX side, in the first 9 months, we have already done a CAPEX of 104 odd crores. Mainly the CAPEX has gone into the fully automatic washing machine project and also into the mobile PLI project, and we expect to close anywhere between 145 to 155 odd crores when we close this financial year. And on the volume side numbers, yes, if I take it segment-wise; LED TV, our volumes were 9 lakhs as against 4.5 lakhs same period last year Q3 versus Q3. There is a growth of almost 100 odd percent. You must have seen that consumer electronics has actually seen a growth of 200 odd percent. Half of that has come through volumes and the balance has come on account of the higher selling prices on the highest category TVs that we are doing. As far as lighting is concerned, if I break it down between LED bulb, batten, downlighters and all - LED bulb, we sold almost 6 crore bulbs; batten, we sold almost 45 lakh battens; downlighters 14 lakhs; and the balance, others which is drivers, was around 26-27 lakhs. Washing machines, we sold around 2.4 lakhs. Overall mobile phones, we sold around 75 lakhs which majorly 72 lakhs were feature phones and 3 lakh smartphones. Of course, this number of smartphones will keep increasing under the PLI. In terms of CCTV, we sold around 9 lakh units and DVR was around 2 lakhs. Set up box, as we mentioned earlier, it was 9 lakhs for the quarter. The RT-PCR machine for Molbio was around 450 units for this quarter.

Moderator:

The next question is from the line of Renu Baid from IIFL. Please go ahead.

Renu Baid:

Good evening and congratulations for strong performance, sir. Two questions. First, given that our core business is having much wider growth opportunities and new business segments are opening up - be it mobile phones, set top boxes, something on cards for laptop and tablets as well. As a company, how are we building our teams and capabilities and leadership to manage growth across all these businesses and drive long-term sustainability? So, first would be just to understand more on the people's side - what are we doing and how are we helping to build the organization as far more robustly?

And second would be, the way we have seen opportunities opening up on the mobile phone side, on the telecom or related equipments, if we see the laptop and tablet segment, what would

be our right to win business in this segment, and as markets open up, to what extent you would be willing to invest in this business?

Atul B Lall:

Responding to your first question, Renu, talent acquisition is presently an extremely important and a focused exercise. Let me assure you, although it's not easy and it's very challenging, we have strengthened our HR department. We have brought in senior people at the level of General Manager from an extremely good organization. We have put our HR processes in place and we are really strengthening our senior and middle management team across all the functions. Whether it is design, expertise in tooling and metal, expertise in manufacturing, the latest quality management systems, IT and manufacturing engineering systems, all across, we are recruiting. In mobile, we have tied up with a global consultant who was the global manufacturing head with one of the largest EMS companies in the Far East, who will be guiding us in this graduating of our program.

It's not easy but I am extremely conscious of it and raised a very pertinent question. These are faiths we are strongly pursuing it. Apart from it, we are also strengthening our IT processes and we have engaged EY for writing a blue book and defining our processes.

Further, at the board level, we have also expanded our board. And yeah, you will be hearing something soon. All that is happening.

You talked about the new opportunities of PLI. Yeah, we are very closely looking at both IT and wearable's PLI because that's a part of our core competence. Let the PLI be announced and we will be definitely pursuing it. In the case of wearables, we already have a partner in boAt. So, we already have an anchor customer. And in the case of IT PLI, also we have a relationship with a large IT player. So, let us see how it pans out but we will be closely pursuing.

Renu Baid:

If you understand here, at least for laptops and tablets, those of initial stage, relationship with Moto or Lenovo could come handy to expand this new portfolio for us?

Atul B Lall:

Renu, I am not in a position to respond to that, but we will definitely be pursuing that.

Moderator:

The next question is from the line of Bharat Shah from ASK Investment Managers. Please go ahead.

Bharat Shah:

In the earlier part of your comments, you mentioned about cost and technology global leadership. Were your comments confined to lighting alone or it extended to more?

Atul B Lall:

Mr. Shah, first of course, I was referring to lighting because in lighting we feel that we have already reached a certain level wherein we can venture into the global markets, wherein we have already started, and we are getting a very positive response from the customers. The second vertical I am referring to wherein we are a strong ODM player is washing machine solutions, fully automatic top loading. The product portfolio that we have which is going to be

launched in the next 3 months and also the cost structures and the industrial footprint in Tirupati campus just being 125 km away from Chennai port and also the numbers in the research work that we have done, we feel confident that 6 to 8 quarters down the line, it opens up a global market for us. So, I was referring to these 2 product solutions.

Bharat Shah:

You correctly reiterated the 3 pillars of your strategy which is to grow the business and earnings, to improve upon working capital efficiency, and to be very prudent and wise about capital allocation and raising capital efficiency bar. On the first part of that earnings expansion, would you be able to give a broad idea of the size of opportunity of which of the categories we are having our share today and what kind of outcome do you think in 3 to 5 years we can expect in each of those categories?

Atul B Lall:

Responding to each category, I will start with lighting. Please appreciate Dixon is somewhere around 1300 to 1500 crores revenue range. The LED bulb alone with the global market is approximately \$8 billion. We are globally competitive. We have the complete product portfolio with us. We are #3 or #4 globally as far as the LED bulb volumes are concerned. The markets and the customers are looking at China + 1 sourcing. So, even if you are able to get 7% to 8% of that LED bulb global market, we are talking about adding approximately \$500 million through the lighting revenue itself over the next 4 to 5 years. Same is the case with washers. When you are able to achieve the global level competitiveness and in-house designing strength and some scale for depending on the domestic market, then you keep on pursuing the global market. And there is a definitive shift in the global industrial footprint wherein the alternates are being looked at. Our large anchor customers are already sending some kind of feelers in that direction. It is not going to happen very soon. It is going to be having a lot of deliverable and execution challenges, but let me assure you, this is the path we are going to pursue.

In the case of mobiles, yeah, we are depending on the PLI and our anchor relationships which is going to take us global right from the year 1. And we are going to be working upon that we stand on our own feet in the next 3 to 4 years with some level of backward integration and also some foray into the ODM part for basic 4G phones. These 3 verticals we will definitely pursue for achieving some kind of global competitiveness and a position in the global markets. Others are a part of the government policy interventions wherein all of us are of a firm conviction that now the electronic products being sold in India would be manufactured in India. And we will keep on grabbing it provided it falls into our filtration criteria of scalability, backward integration, migration to ODM, and low on capital intensity. It is very difficult to give me the numbers but think the opportunity is extremely healthy.

Moderator:

The next question is from the line of Sonali Salgaonkar from Jefferies India. Please go ahead.

Sonali Salgaonkar:

Congratulations on a great set of numbers. Sir, my first question is, with the business mix changing more towards mobile phones and consumer electronics, because of the new customer

additions, what could be the steady state operating margin that we should look at going forward?

Saurabh Gupta:

Sonali, your observation is absolutely right. I think so both these businesses as a percentage of revenues will start contributing more and you will see that in the next fiscal also. I see mobiles and EMS divisions start contributing almost 35% to 40% of our revenues next year. Similarly, if I look at and extrapolate this trend of consumer electronics as well where we have a strong order book and we are adding more customers there and the market is also shifting to 43 inches and above, then clearly the consumer electronics in terms of revenues would also be higher. So, my sense is, what you see in this quarter, the kind of EBITDA margins which have come down - of course, absolute EBITDA has grown significantly but the EBITDA margins which have come down to 4.6%, I think so that should be the going run rate for the next fiscal year as well. So, between a plus or minus 4.5% to 4.7% kind of a range, that will be the going rate for EBITDA margins.

Sonali Salgaonkar:

Sir, my second question is more from a strategy perspective. Our ODM share right now is about 35% of our revenue mix. With so many new opportunities opening up for us, more in the design space, where do we foresee that ODM share to reach at, say, over the next 3 to 5 years?

Atul B Lall:

In the next year or a couple of years, ODM as a percentage of revenue would be lower because the maximum growth is coming in, the outlier is going to be mobile phones which is on a prescriptive mode and LED televisions which again largely is on a prescriptive mode. LED televisions to start with, we are in discussions for some JDM kind of business. I have a strong conviction that somewhere mid next year, we should be able to have some breakthroughs with some large customers. If that happens, I feel the ODM share in televisions is going to go up to almost 15% to 20%. Mobiles would continue to be prescriptive for at least a couple of years to come. LED lighting is already at 91% to 92% of ODM which further I think is going to increase to 95% to 96% because more growth is going to come from the ODM side only. And appliances in any case is 100% ODM. The other strategic thing whether it is.... set top boxes, again, a part of it is going to migrate to JDM. In the case of medical electronics and wearables to start with is all going to be prescriptive. So, I don't have a number as such in hand and that how it is going to be panned out, but the overall profile of ODM versus OEM in respective verticals is what I am sharing with you.

Sonali Salgaonkar:

Lastly, what could be the steady state CAPEX outlay that we could expect over the next 3 to 4 years?

Saurabh Gupta:

Sonali, we have mapped out our cash flows, CAPEX, and the source of funding for the next 15 months. My sense is, as I mentioned, this year our CAPEX we will be closing somewhere around 145 to 155 odd crores and similar will be the going run rate for the next financial year as well. So, at least for the next financial year, the CAPEX would be almost similar to this year.

- Moderator:** The next question is from the line of Nitin. Please go ahead.
- Nitin:** There is one question in terms of as the business is now scaling up growing at about 20 odd percent or more, what are the supply chain issues that could emerge for you or for the country? What makes you worried on the supply chain in terms of component availability? And are you seeing any progress related to this - investments on the supply chain components in India through the ecosystem of these large brands which are giving you big business?
- Atul B Lall:** Nitin, the present supply chain challenges are primarily on the glass side which is impacting both the open cell supply for televisions and display for mobiles. Some of the basic glass panels of LG and Corning have had a shutdown and also at the open cell level, there has been some restructuring on the industry side. So, I feel that in the current quarter and the Q1 of next fiscal, this kind of pain will continue. Post that, we are expecting the glass furnaces to revive by that time and there should be some smoothening of the supplies of glass, both for display as well as the open cell from Q2 of the next fiscal.
- On the semiconductor and the IC side, there is a significant shortage. One, because of the geopolitical situation, certain brands which were put under pressure - it mopped off a lot of inventory - and also a lot of semiconductor production and IC production is going in for the EV side because of better margins there. So, I feel that at least for a couple of quarters more till the time the new capacities come up, the pain point on the driver IC side, on the microprocessor side, and also on the semiconductor side will continue. That is the situation.
- Nitin:** Any investment in this context happening in India at the ecosystem?
- Atul B Lall:** Not in India, I don't foresee that.
- Nitin:** Sir, the second question was about the competition. When you are working with these global brands for wash or for that matter in mobiles now in Motorola, I know India lacks competing capacities to you, but what are the other alternatives that these brands are considering? Are these like Turkish players or Vietnamese? Who are the alternatives for China + 1 which are also trying their hand?
- Atul B Lall:** The main competition is from Vietnam. In fact, they have bagged a very large share of the global supply chain in electronics, whether it is mobiles or other electronic products. So, undoubtedly it is Vietnam. Beyond Vietnam, I see the next option being very seriously evaluated by large global players is India. I have seen that the large companies which had their base in Thailand, they are also looking at India, which had their base in Philippines are also looking at India. So, I would say in that order - China and then Vietnam and then India.
- Nitin:** Where does Vietnam score higher than India, in what aspects?
- Atul B Lall:** It already has a very large scale because if you see the global exports from India of electronics, it is somewhere around \$6 billion to \$7 billion and Vietnam has already had somewhere

around \$100 billion. You see the footprint of Samsung there. Samsung management is treated like a royal guest there.

Vietnam already is much ahead because the ecosystem has already been developed there. They all have problem from limited manpower. So, I don't think it can replicate completely what China is but there have definitely be an overflow to other countries and which India stands a very strong now.

Nitin: Sir, what I was asking a question was on the labor cost on a per head product piece basis or power cost, or logistics cost, is India getting on any factor better than Vietnam so that incrementally the share of India can be higher?

Atul B Lall: On the labor cost side, India is better both on the cost and the productivity side. Productivity side we match them, and the cost is lower, and the power tariff is same, but there would be some disability on the infrastructure side and on the land side.

Moderator: Ladies and gentlemen, due to time constraints, that would be our last question for today. I would now like to hand the conference over to the management for their closing remarks. Thank you and over to you.

Atul B Lall: Thanks everyone.

Saurabh Gupta: Thank you everybody.

Moderator: Ladies and gentlemen, on behalf of Ambit Capital, that concludes today's call. Thank you all for joining us, and you may now disconnect your lines.